



Audit Report



OIG-07-011

Audit of the Community Development Financial Institutions
Fund's Fiscal Years 2006 and 2005 Financial Statements

November 15, 2006

Office of
Inspector General

Department of the Treasury



OFFICE OF
INSPECTOR GENERAL

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

November 15, 2006

**MEMORANDUM FOR ARTHUR A. GARCIA, DIRECTOR
COMMUNITY DEVELOPMENT FINANCIAL
INSTITUTIONS FUND**

FROM: Michael Fitzgerald *Michael Fitzgerald*
Acting Deputy Assistant Inspector General
for Financial Management and Information
Technology Audits

SUBJECT: Audit of the Community Development Financial Institutions
Fund's Fiscal Years 2006 and 2005 Financial Statements

I am pleased to transmit the attached audited Community Development Financial Institutions Fund (CDFI) financial statements for fiscal years 2006 and 2005. We contracted with the independent certified public accounting firm KPMG LLP to audit the financial statements of CDFI as of September 30, 2006 and 2005, and for the years then ended. The contract required that the audit be performed in accordance with generally accepted government auditing standards; applicable provisions of Office of Management and Budget Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*; and the *GAO/PCIE Financial Audit Manual*.

The following reports, prepared by KPMG LLP, are incorporated in the attachment:

- Independent Auditors' Report;
- Independent Auditors' Report on Internal Controls; and
- Independent Auditors' Report on Compliance and Other Matters

In its audit, KPMG LLP found that the financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. However, KPMG LLP's Report on Internal Controls contained two reportable conditions related to controls over accounting for software-in-development and grants monitoring, which were not considered material weaknesses. Further, KPMG LLP found one instance of reportable noncompliance with laws and regulations, related to noncompliance with the Single Audit Act Amendments of 1996.

KPMG LLP also issued a management letter dated November 8, 2006, discussing other matters involving internal control over financial reporting and its operation that were identified during the audit but were not required to be included in the auditors' reports.

In connection with the contract, we reviewed KPMG LLP's reports and related documentation and inquired of its representatives. Our review, as differentiated from an audit in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on the financial statements or conclusions about the effectiveness of internal control or compliance with laws and regulations. KPMG LLP is responsible for the attached auditors' reports dated November 8, 2006 and the conclusions expressed in the reports. However, our review disclosed no instances where KPMG LLP did not comply, in all material respects, with generally accepted government auditing standards.

Should you have any questions, please contact me at (202) 927-5789.

Attachment

Community Development Financial Institutions Fund

U.S. Department of the Treasury



Performance and Accountability Report

FY 2006

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MESSAGE FROM THE DIRECTOR

I am pleased to present the Community Development Financial Institutions Fund's Performance and Accountability Report for Fiscal Year 2006. Through the Fund's mission of expanding the availability of credit, investment capital, and financial services in distressed urban and rural communities, the Fund continues to deliver programs and funding that provides deliverable results to the communities that are in the greatest need.

Our vision is an America in which all people have adequate access to affordable capital, credit and financial services. The CDFI Fund makes this possible by investing in and building the capacity of a nationwide network of community-based, private, for-profit and non-profit financial institutions with a primary mission of community development in economically distressed urban, rural and Native communities. These institutions – certified by the CDFI Fund as community development financial institutions - are able to respond to gaps in local markets that traditional financial institutions are not adequately serving. They provide a wide range of financial products and services including: mortgage financing for first time home buyers, financing for needed community facilities, commercial loans and investments to start or expand small businesses, loans to rehabilitate rental housing and financial services needed by low income households and local businesses.

The CDFI Fund continues to try and improve the economic and living conditions of underserved communities. This past year continued to be one of improvement and focused on increasing the Fund's investment in community development activities through its programs. I am pleased to report that all program awards were delivered on schedule. The CDFI Fund's outlook for the 2007 fiscal year will be for the efficient delivery of all program awards as funding is appropriated. The CDFI Fund's 2006 Performance and Accountability Report marks the ninth consecutive year in which the auditors rendered an unqualified opinion on the CDFI Fund's financial statements and in which no material weaknesses were reported.

All of this has been made possible by the CDFI Fund staff and their commitment to serving low-income communities and individuals. I would like to thank them again for their service to the Fund.

A handwritten signature in black ink, appearing to read 'Arthur Garcia', is positioned above the printed name and title.

**Arthur Garcia,
Director**

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND OVERVIEW

The Community Development Financial Institutions Fund (the Fund) was created for the purpose of promoting economic revitalization and community development through investment in and assistance to community development financial institutions (CDFIs). The Fund's role in promoting community and economic development was expanded in FY 2001 when the Secretary of the Treasury delegated to the Fund the responsibility of administering the New Markets Tax Credit (NMTC) Program. Since its creation in 1994, the Fund has awarded \$820 million to CDFIs, community development organizations and financial institutions through the Community Development Financial Institutions (CDFI) Program, the Bank Enterprise Award (BEA) Program, and its Native Initiatives. In addition, the Fund has allocated \$12.1 billion in tax credit authority to community development entities (CDEs) through the NMTC Program.

Authorizing Legislation

The Fund was established as a bipartisan initiative under the Riegle Community Development and Regulatory Improvement Act of 1994. The NMTC Program was authorized through the Community Renewal Tax Relief Act of 2000.

Fund's Mission

The Fund's vision is an America in which all people have access to affordable credit, capital and financial services. Its mission is to expand the capacity of financial institutions to provide credit, capital, and financial services to underserved populations and economically distressed communities in the United States.

The Fund achieves its purpose by promoting access to capital and local economic growth through:

- 1) the **CDFI Program**, by making funding available to financial institutions that are certified or eligible to be certified as CDFIs, which in turn provide loans, investments, financial services and technical assistance to underserved populations and low-income communities;

- 2) the **NMTC Program**, which provides tax allocation authority to CDEs, enabling investors in these CDEs to claim tax credits against their Federal income taxes and the CDEs, in turn, use the capital raised to make investments in low-income communities;
- 3) the **BEA Program**, which provides cash awards to banks for increasing their investment in low-income communities and/or in CDFIs; and
- 4) **Native Initiatives**, which provides financial assistance, technical assistance, and training to Native CDFIs and other Native entities proposing to become or create Native CDFIs.

What is a CDFI?

Generally, CDFIs are community-based specialized financial institutions that serve low-income people or work in economically distressed communities, often working in market niches that may be underserved by traditional financial institutions. Only financial institutions certified by the CDFI Fund can receive funding through the CDFI Program and Native Initiatives (certain other entities can receive an awards through the Native Initiatives).

CDFIs seek to provide a unique and wide range of financial products and services that may help their customers build wealth and achieve the goal of participating in the ownership society. While the types of products made available may be similar to those provided by larger mainstream financial institutions (such as mortgage financing for low-income and first-time homebuyers, small business lending, and lending for community facilities), CDFIs generally lend to and make equity investments in markets not served by traditional financial institutions. CDFIs may offer rates and terms that are more flexible than those provided by traditional financial institutions. CDFIs also seek to provide services that will help ensure that credit is used effectively, such as technical assistance to small businesses and credit counseling to consumers. CDFIs include regulated institutions such as community development banks and credit unions, and non-regulated institutions such as loan funds and venture capital funds, among others.

Certification of Community Development Financial Institutions and Community Development Entities

CDFI certification is a designation conferred by the Fund. An organization that meets six statutory and regulatory criteria (as listed in the “Community Development Financial Industry” section) may be certified as a CDFI. The certification is a requirement for accessing a financial assistance award from the Fund through the CDFI Program and the Native American CDFI Assistance (NACA) Program, and certain benefits through the BEA Program. As of September 30, 2006 there were 762 Certified CDFIs.

A Community Development Entity (CDE) is a domestic corporation or partnership that is an intermediary vehicle for the provision of loans, investments, or financial counseling in low-income communities through the NMTC Program. CDEs must demonstrate a primary mission of serving low-income communities and low-income persons, and must demonstrate that they are accountable (through representation on a governing board or advisory board) to residents of low-income communities. CDEs are certified as such by the Fund and are eligible to apply for tax credit allocations through the NMTC Program.

Many CDEs create multiple subsidiary CDEs to own specific assets or classes of assets, and thus the number of CDEs has grown to 2,294 as of September 30, 2006. Benefits of being certified as a CDE include being able to: (1) apply to the Fund to receive a NMTC allocation to offer to its investors in exchange for equity investments in the CDE and/or its subsidiaries; or (2) receive loans or investments from other CDEs that have received a NMTC Allocation. CDEs must be certified to receive allocations of tax credits.

Growth in Number of Certified CDFIs and CDEs

<u>End of FY</u>	<u>CDFIs</u>	<u>CDEs</u>
1997	190	
1998	262	-
1999	334	-
2000	415	-
2001	468	31
2002	625	541
2003	694	1,184
2004	728	1,585
2005	752	1,954
2006	762	2,294

CDEs are located in 49 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands. CDFIs are located in every state the District of Columbia, Puerto Rico and the U.S. Virgin Islands.

Summary of the Fund’s Programs

The Fund’s programs are summarized below. More detailed information on each program can be found in the related section of the *Program Discussion and Analysis* section of this report.

Community Development Financial Institutions

Program: *Performance Goal: Build the capacity and coverage of CDFIs to provide credit, capital, and related services to otherwise underserved markets.*

Through the CDFI Program, the Fund provides financial assistance in the form of grants, loans, and equity investments to CDFIs and technical assistance grants to CDFIs and entities that plan to become CDFIs.

- **Financial Assistance (FA)** awards, in the form of grants, loans, and equity investments, to CDFIs that have comprehensive business plans for creating community development impact and that demonstrate the ability to leverage private sector sources of capital.
- **Technical Assistance (TA)** awards to CDFIs and entities proposing to become CDFIs in order to build their capacity to advance community development and meet capital access needs in their target markets. Technical Assistance awards can also be accessed by larger and more established CDFIs to support their continued development.

New Markets Tax Credit Program: *Performance Goal: Attract private sector capital into low-income communities through CDEs.*

The NMTC Program is intended to spur the investment of new private sector capital into low-income areas through CDEs, which in turn use the privately managed investment vehicles to make loans and equity investments in businesses and real estate projects in low-income communities. The NMTC Program was authorized under the Community Renewal Tax Relief Act of 2000. The statute included \$15 billion in allocation authority for seven years. Under the Hurricane Katrina Gulf Opportunity (GO) Zone Act of 2005 an additional \$1 billion in allocation authority was directed to the rebuilding and renewal of the GO

Zone. By making an equity investment in a CDE, individual and corporate investors can receive a tax credit against their Federal income taxes worth 39 percent of the value of the amount invested in the CDE over 7 years.

Calendar Year 2002 was the first year in which applications for NMTC were submitted to the Fund and, as of the end of FY 2006 four allocation rounds have been completed providing allocations of tax credit authority that will support, in the aggregate, equity investments of \$12.1 billion (including \$600 million for GO Zone allocations). One more allocation round remains through which the Fund will allocate tax credit authority supporting \$3.5 billion in investor capital plus an additional \$400 million of tax credit authority for use in the GO Zone.

Bank Enterprise Award Program: *Performance Goal: Increase FDIC-insured institutions' investments in community development and economic revitalization in distressed communities.*

The Bank Enterprise Award (BEA) Program recognizes the key role played by traditional financial institutions in community development lending and investing. Through the BEA Program, the Fund provides monetary awards to regulated banks and thrifts for increasing their investments and financial activities in economically distressed communities (those with high poverty and unemployment) and/or investments in CDFIs. The size of the award is a percentage of the increase in activities from one annual reporting period to the next.

Native Initiatives: *Performance Goal: Build the capacity and coverage of CDFIs and other institutions to provide credit, capital, and related services to Native Communities.*

The Fund's Native Initiatives are intended to assist entities in overcoming barriers that prevent access to credit, capital and financial services in Native American, Alaskan Native and Native Hawaiian communities. The central program of the Native Initiatives is the Native American CDFI Assistance (NACA) Program, which is targeted to increasing the number and capacity of existing or new CDFIs that serve Native Communities. In addition, the Native Initiatives includes training that seeks to foster the strengthening or development of Native CDFIs. In FY 2006, the Fund initiated two contracts that will result in additional training and technical assistance through the Native Initiatives.

Performance Measures: This Performance and Accountability report includes a discussion of those performance measures the Fund considers the most significant. For a discussion about all of the Fund's performance measures, see the applicable appendix in the *FY 2006 Performance and Accountability Report* for the Department of the Treasury.

Allocation of Funding

The Fund's appropriations comprise program funds and administrative funds. Program funds are amounts that are used for program awards (such as grants, loans, equity investments, and training contracts); administrative funds are amounts used to cover the costs to administer all programs (including the NMTC Program).

As noted above, the Secretary has delegated authority to the Fund to allocate tax credits through the NMTC Program. As NMTCs are not monetary awards, they are not reflected in the chart below. The NMTC funding as shown in the chart represents program administration costs.

Sources of Funding

Congress appropriates funds annually to the Fund; each appropriation can be used over two fiscal years. Appropriations include fiscal year budget authority and, if any unobligated funds from the prior year carryover. The annual appropriation amount includes borrowing authority to make loans.

Sources of Funding (amounts in millions)		
	<u>FY 2006</u>	<u>FY 2005</u>
Appropriations (1)	\$54.5	\$ 55.6
Use of No-Year Account (2)	1.3	4.0
Amounts Deobligated	1.0	1.2
Carryover from Prior Year	3.0	.8
Borrowing Authority Used	<u>.6</u>	<u>3.6</u>
Total Sources of Funds	<u>\$60.4</u>	<u>\$ 65.2</u>
(1) FY 2005 includes \$.5 million pertaining to upward subsidy adjustment.		
(2) The No-Year account consist of investment income, and proceeds from the redemption of investments.		

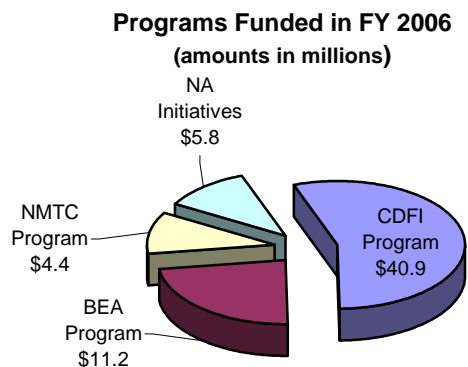
Uses of Funding

During FY 2006, the Fund used funding of \$60.4 million as follows:

Uses of Funding (amounts in millions)		
	<u>FY 2006</u>	<u>FY 2005</u>
Programs Funded		
CDFI Program	\$32.8	\$40.9
BEA Program	13.7	11.2
NMTC Program	6.2	4.4
Native Initiatives	<u>6.6</u>	<u>5.8</u>
Total Programs Funded	\$59.3	\$62.3
Amounts Not Obligated (1)	<u>1.1</u>	<u>2.9</u>
Total Funding Used	<u>\$60.4</u>	<u>\$65.2</u>

Note – administrative funds of \$15.4 million and \$13.5 million have been allocated to the above programs for FY 2006 and 2005, respectively.

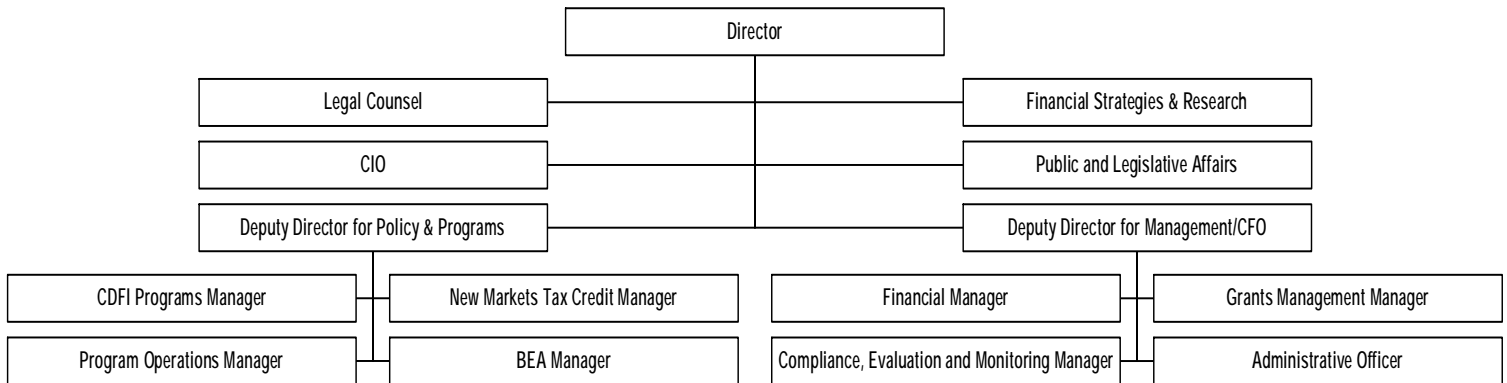
(1) – FY 2005 amounts not obligated includes \$2.1 million earmarked for an evaluation of the NMTC Program which is included in the FY 2006 NMTC Program amount.



ORGANIZATION OF THE FUND

The Fund's organization structure consists of a Director, a Deputy Director for Policy and Programs, a Deputy Director for Management / Chief Financial Officer, Manager for Public and Legislative Affairs, Legal Counsel, Chief Information Officer (CIO), and various program and administrative support offices. The organization chart of the Fund is shown below.

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND SEPTEMBER 2006



Program Discussion and Analysis

OVERVIEW OF THE CDFI PROGRAM

Through the Community Development Financial Institutions (CDFI) Program, the Fund uses federal resources to invest in and build the capacity of CDFIs to serve low-income people and communities lacking adequate access to affordable financial products and services. The Fund provides monetary awards for financial assistance (FA) and technical assistance (TA) grants through its CDFI Program. CDFIs use FA awards to further goals such as:

- Economic development (job creation, business development, and commercial real estate development);
- Affordable housing (housing development and homeownership); and
- Community development financial services (provision of basic banking services to underserved communities and financial literacy training).

Certified CDFIs

A certified CDFI is one that has been certified by the Fund as meeting all of the following statutory and regulatory criteria:

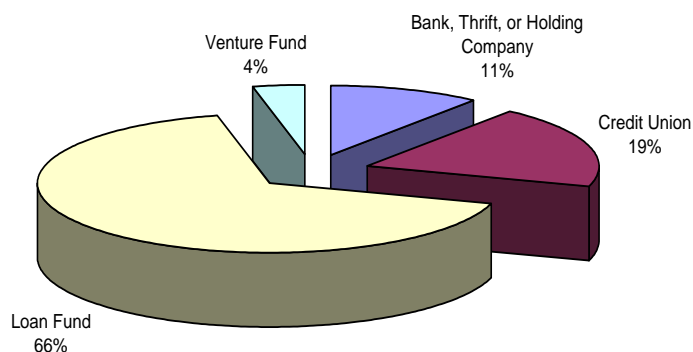
- Has a primary mission of promoting community development;
- Serves principally an investment area or targeted population;
- Is an insured depository institution, or makes loans or development investments as its predominant business activity;
- Provides development services (such as technical assistance or counseling) in conjunction with its financing activity;
- Maintains accountability to its target market; and
- Is a non-governmental entity and cannot be controlled by any governmental entities.

In addition to seeking certification to receive financial and technical assistance from the Fund, organizations pursue CDFI certification in order to leverage funds from non-federal sources such as banks, foundations, and state and local governments.

The certification of organizations as CDFIs has been a long-standing goal of the Fund. By the end of FY 2006, the Fund had certified 762 CDFIs serving both rural and urban areas in all states and the District of

Columbia, Puerto Rico, and the Virgin Islands. The majority of certified CDFIs as of the end of FY 2006 are loan funds and credit unions. Far smaller percentages are banks, thrifts and depository holding companies, and venture funds. The below percentages are very similar to those as of the end of the prior year.

Breakdown of Types of Certified CDFIs



Not surprisingly, the most populous states have the most certified CDFIs: 28 percent of certified CDFIs are headquartered in the five most populous states (New York, Texas, North Carolina, Florida and California)

CDFIs include banks, credit unions, loan funds, and venture capital funds, with each providing a different mix of products geared to reach specific customers, as follows:

- Community development banks are for-profit corporations which provide capital to rebuild economically distressed communities through targeted lending and investment;
- Community development credit unions are non-profit cooperatives owned by members which promote ownership of assets and savings and provide affordable credit and retail financial services to low-income people;
- Community development loan funds (usually non-profits) provide financing and development services to businesses, organizations and individuals in low-income urban and rural areas and can be further categorized based on the type of client served: micro-enterprise, small business, housing and community service organizations; and

- Community development venture capital funds are both profit and non-profit organizations which provide equity and debt-with-equity features for businesses in distressed communities.

CDFI Customers

CDFI customers consist of the following:

- Small business owners who provide employment opportunities and needed services to disadvantaged communities;
- Affordable housing developers that construct and rehabilitate homes in low-income communities;
- Community facilities that provide child care, health care, education and social services in underserved communities;
- Commercial real estate developers that finance the acquisition, construction or rehabilitation of retail, office, industrial and community facility space in low-income communities; and
- Individuals who are provided affordable banking services including checking and savings accounts, alternatives to predatory financial companies, and mortgages and other kinds of loans.

Financial Assistance Component

The CDFI Program consists of two components: the Financial Assistance (FA) Component, which is by far the largest component of the program, and the Technical Assistance (TA) Component. Prior to FY 2003, the FA Component was referred to as the Core Component. Through the FA Component, the Fund invests in CDFIs that are able to demonstrate that they have the financial and managerial capacity to provide affordable and appropriate financial products and services that positively impact their communities, are viable financial institutions, and use and leverage Fund dollars effectively.

Through the CDFI Program, the CDFI Fund invests in and supports community-based organizations, known as community development financial institutions - or CDFIs – that provide financing and related services to communities and populations that lack access to credit, capital and financial services. Applicants can apply for financial assistance only, technical assistance only, or a combination of both financial assistance and technical

assistance through this single application. Those applicants applying for financial assistance will have to indicate which of two categories types it is applying under: Category 1 – Small and Emerging CDFI Assistance (SECA); and Category 2 – Core.

FA awards are made in the form of equity investments, loans, deposits, or grants, depending on applicant needs, and must be matched by the applicant with funds of the same type from non-federal sources. FA awards enable CDFIs to leverage private capital to respond to demand for affordable financial products and services in economically distressed markets and by low-income families. CDFIs respond to this demand through the provision of loans, investments, training, technical assistance and basic financial services such as checking or savings accounts. Based on data supplied by CDFIs required to report to the Fund, it is estimated that CDFIs leverage their FA awards with other dollars by an average of 27:1.

FY 2006 Changes to the Financial Assistance Component

The Fund's 2006 Notice of Funds Availability (NOFA) combined FA and TA and issued the NOFA for two funding rounds (FY 2006 and FY 2007).

Combine the FA Component and the TA Component into a single CDFI Program NOFA and application: The CDFI Program NOFA was published concurrent with the NACA (Native American CDFI Assistance) Program NOFA. The CDFI Program application and the NACA Program application generally have the same questions. The result is greater clarity for applicants and a demonstration that the Fund has consistency and similar policies across its programs.

Make Uses of TA Awards consistent with NACA Program: The CDFI Fund made the CDFI Program consistent with the NACA Program by making recurring tasks and expenses eligible uses of TA. The Fund decided to follow the structure established by NACA by: (i) applying a \$100,000 cap; (ii) allowing any use eligible by OMB; (iii) making the category eligible for all applicants; (iv) requiring the applicant to submit a budget; and (v) requiring the applicant to demonstrate how the use would strengthen its capacity to serve its market, create impact, build the infrastructure of the organization, or allow the applicant to hire a key staff person.

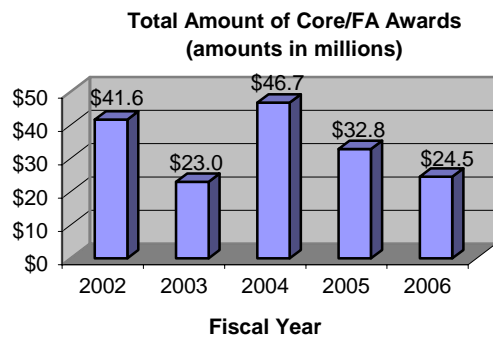
Implementation of Grants.gov: In FY 2006 the CDFI Program began to use Grants.gov. The Fund is using Grants.gov to be consistent with the Federal government's effort to streamline the process for applying for Federal grants and to improve public access to funding opportunities.

Applicants go to the Grants.gov website, register as a user and download the application materials. They complete the application materials offline using Word or Excel templates. They complete the Standard Form 424 Application for Federal Assistance. Once all application materials are complete, applicants submit them via Grants.gov and mail any paper attachments.

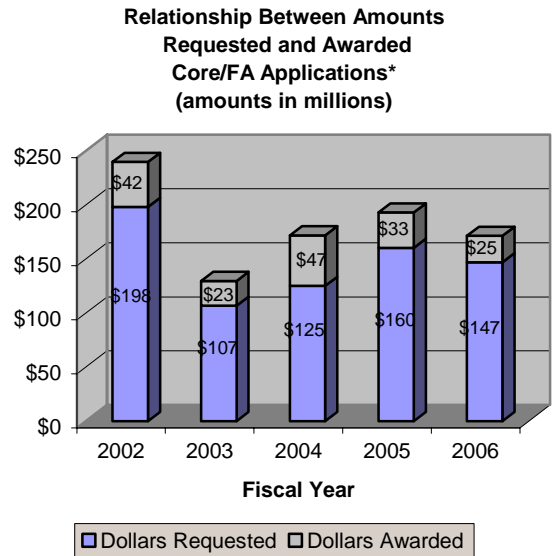
FY 2006 Awards

During FY 2006, the Fund received 127 applications requesting \$146.7 million in Financial Assistance, including 41 SECA applicants requesting \$18.2 million.

FA awards totaling \$24.47 million were made to 52 organizations, compared to \$32.8 million made to 48 organizations in the prior year. The FY 2005 awards included 17 awards totaling \$4.2 million to SECA applicants.



The significant difference between the FY 2003 and FY 2004 amounts above was due to program changes made in FY 2003, resulting in a smaller number of applications received that year. Amounts not awarded during FY 2003 were carried over and awarded in FY 2004. The reduction in FA awards from FY 2004 to FY 2005 is attributable to these additional awards made in FY 2004 combined with a \$5 million reduction in appropriated dollars for FY 2005. The FY 2006 award amount reflects the appropriated dollars for that year. In the bar chart below, the amount requested was \$146.7 million and the amount awarded was \$24.47 in FA.



* FY 2003 and FY 2004 amounts consist of FA applications and awards; Core applications and awards are prior to FY 2003.

Technical Assistance Component

The Technical Assistance (TA) Component provides grants to build the capacity of start-up and existing CDFIs by acquiring prescribed types of products or services including technology (usually efficiency enhancing technology such as computers and loan management software), staff training, consulting services to acquire needed skills or services (such as a market analysis or lending policies and procedures), or staff time to conduct discrete, capacity-building activities (such as website development).

More established CDFIs also use TA grants to build their capacity to provide new products, serve current markets in new ways, or enhance the efficiency of their operations; examples include upgrading computer hardware and software.

TA awards have a "soft cap," generally limiting awards to no more than \$50,000. The average award for this round was approximately \$50,000 (several awards were higher than the soft cap).

FY 2006 Changes to the Technical Assistance Component

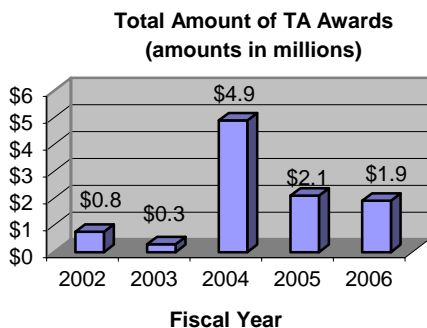
The Fund's 2006 NOFA combined FA and TA and issued the NOFA for two funding rounds (FY 2006 and FY 2007).

The FY 2005 NOFA encouraged applicants to request TA to improve their ability to collect performance data effectively and monitor the community impact of their activities. The application included a new section designed to assist applicants to assess their current data collection capabilities and identify which, if any, categories of TA are needed to support this capacity development.

FY 2006 Awards

In FY 2006, the Fund received 53 applications requesting \$3.4 million in TA grants of which \$1.91 million was awarded to 21 organizations, compared to the \$2.1 million awarded to 41 organizations during FY 2005.

Of the 21 organizations receiving TA awards, 27% were funded to increase the efficiency and capacity of their organizations through the addition or expansion of technology. Total award dollars to these awardees was \$517,100.



CDFI Program Performance

CDFI Program awardees report their annual performance to the Fund through the Fund's web-based reporting system, the Community Investment Impact System (CIIS). Each awardee has 180 days from its fiscal year end to report through CIIS. This time allows the awardee to complete its annual audit and enables the

Fund to verify reported information against the audit. The performance information provided herein pertains to each awardee's 2005 fiscal year. It should also be noted that due to the length of time from notice of award through award disbursement, award deployment by an awardee, and receipt by the Fund of awardee impact information, the effect of the Fund's awards made during any given year is not known until quite some time later.

Results based on information entered into CIIS by 186 CDFI Program awardees are shown in the table below:

Performance of 186 CDFI Program Awardees During FY 2005*	
1. # of full time jobs created or maintained (57)	13,777
2. # of businesses financed (72)	2,694
3. # of commercial real estate properties financed (31)	274
4. # of affordable housing units financed (52)	26,832
5. # of homebuyers who obtain financing (40)	2,196
6. # of accounts opened to the unbanked (9)	13,992
7. Dollars leveraged with private investments	\$1.4 billion
8. # of individuals provided with financial literacy and other training (165)	147,787
9. Individual Development Accounts (IDAs) provided by CDFIs (29):	
Number	2,562
Dollar amount	\$5.2 million

* As of the date this report was produced, the Fund had not completed the "cleansing" process for CIIS data. During cleansing, the Fund reviews the data for consistency with the CDFI's financial statements and overall reasonableness. The data in this table represent 81cleansed and 105 uncleaned CIIS reports. Numbers in parentheses are the number of CDFI awardees reporting on this particular measure.

OVERVIEW OF THE NEW MARKETS TAX CREDIT PROGRAM

The New Markets Tax Credit (NMTC) Program permits taxpayers to receive a credit against Federal income taxes for making qualified equity investments in designated Community Development Entities (CDEs). Substantially all of the qualified equity investment must in turn be used by the CDE to provide investments in low-income communities.

The credit provided to the investor totals 39 percent of the cost of the investment and is claimed over a seven-year credit allowance period. In each of the first three years, the investor receives a credit equal to five percent of the total amount paid for the stock or capital interest at the time of purchase. For the final four years, the value of the credit is six percent annually. Investors may not redeem their investments in CDEs prior to the conclusion of the seven-year period

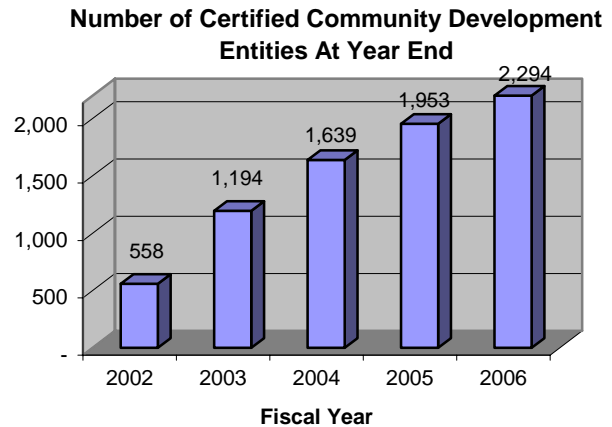
To qualify as a CDE, an entity must be a domestic corporation or partnership that: 1) has a mission of serving, or providing investment capital for, low-income communities or low-income persons; 2) maintains accountability to residents of low-income communities through their representation on a governing board of or advisory board to the entity; and 3) has been certified as a CDE by the CDFI Fund. As of September 30, 2006, 2,294 organizations have been certified as CDEs by the CDFI Fund, compared to 1,953 as of one year earlier.

Results of First Four NMTC Allocation Rounds

Throughout the life of the NMTC Program, the Fund is authorized to allocate to CDEs the authority to issue to their investors up to \$16 billion in equity against which NMTCs can be claimed, including \$1 billion of special allocation authority made available under the Gulf Opportunity (GO) Zone Act of 2005 to be used for the recovery and redevelopment of the Hurricane Katrina GO Zone.

Allocations are awarded annually through a competitive process. To date, the Fund has completed four allocation rounds and has made 233 awards totaling \$12.1 billion in allocation authority, including \$600 million in special GO Zone allocation authority

under the 2006 allocation round. The 2007 allocation round will provide \$3.9 billion in allocation authority, including \$400 million in special GO Zone allocation authority.



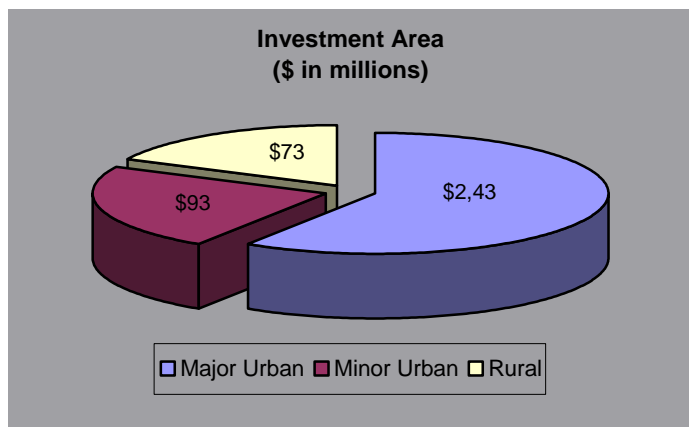
Demand for the tax credits has been high, as 1,078 applicants have requested credits supporting over \$108 billion in equity investments – approximately nine times the amount of allocation authority available for distribution by the CDFI Fund. Through the first four allocation rounds, only 22% of applicants have been selected to receive an award. The average tax credit allocation award through the first four rounds was \$52 million.

Completed Funding Rounds (Dollars in Billions)				
Round	Applications		Allocations	
	Number	Amount	Number	Amount
1	345	\$25.8	66	\$2.5
2	271	\$30.4	63	\$3.5
3	208	\$22.9	41	\$2.0
4	254	\$28.3	63	\$4.1
	1078	\$107.4	233	\$12.1

2006 NMTC Allocation Round (Round 4) Summary

In June of 2006, the CDFI Fund announced that 63 applicants had been awarded \$4.1 billion in NMTC allocation authority, including 13 applicants that were awarded \$600 million for specific use in the recovery and redevelopment of the Hurricane Katrina GO Zone.

The 63 allocatees are headquartered in 19 different states and the District of Columbia, but anticipate making awards in 40 different states, as well as D.C. Based upon information reported by the allocatees, it is anticipated that approximately \$2.43 billion (or 59%) will be invested in major urban areas; approximately \$937 million (or 23%) will be invested in minor urban areas; and approximately \$731 million (or 18%) will be invested in rural areas.



These 63 allocatees have committed to achieving results above and beyond minimal program requirements:

- All 63 of the allocatees indicated that 100% of their investment dollars would be made either in the form of equity, or in the form of debt that is at least 25% below market and/or is characterized by multiple concessionary features. Such features include, among other things, equity-equivalent terms and conditions; subordinated debt; reduced origination fees; and higher than standard loan-to-value ratios.

- Of the 63 allocatees, 56 indicated that at least 90% of their activities will be provided in areas of higher economic distress (and/or areas targeted for development by other government programs) than are minimally required under NMTC Program rules, and 42 indicated that 100% of their activities would be provided in such areas.
- All 63 of the allocatees indicated that they would invest more than the minimally required 85% of QEI dollars into Qualified Low-Income Community Investments (QLICI), and 58 of the 63 allocatees indicated that at least 95% of their QEI dollars would be invested into qualified low-income community investments. In real dollars, this means at least \$477 million above and beyond what is minimally required by the NMTC Program will be invested in low-income communities.

NMTC Activities to Date

Allocation agreements have been executed with each of the 170 allocatees from the first three rounds. As of September 30, 2006, 142 of these 170 allocatees (84 percent) had reported raising QEIs totaling \$4.76 billion.

Allocatees report QEI and QLICI activity to the Fund through the Community Investment Impact System (CIIS). Allocatees that have raised QEIs are required to complete an annual Institution Level Report (ILR) in CIIS. Allocatees that have made QLICIs are also required to submit an annual Transaction Level Report (TLR) in CIIS. An allocatee's ILR, TLR, and audited financial statements are due 180 days after the end of its fiscal year.

All results in this section represent the allocatees' data reported through their FY 2005. As shown in the table below, allocatees reported making \$1.9 billion of loans and investments in QALICBs (Qualified Active Low Income Community Businesses) in FY 2005, and a total of \$3.1 billion of loans and investments in QALICBs since the program's inception. In FY 2005, 77% of the loans and investments in QALICBs supported real estate development or rehabilitation. It is projected that these loans and investments will result in the development or rehabilitation of 25

million square feet of commercial real estate, and the creation of more than 38,000 construction jobs.

The remaining 23 percent of the loans and investments to QALICBs were made to operating businesses in low-income communities. The businesses financed by allocatees created or maintain nearly 9,000 Full Time Equivalent (FTE) jobs in FY 2005 alone. Finally, the allocatees reported that 98 percent of the loans and investments they provided in FY 2005 had better rates and terms than could be offered in the prevailing market.

In FY 2005, allocatees also reported making over \$10 million in direct investments into other CDEs, purchasing \$51 million in loans from other CDEs, and providing financial counseling and other services to 316 businesses in low-income communities.

(Note: Table on following page).

Performance of 103 NMTC Allocatees

Type of QLICI

QALICB: Real Estate Development and Rehabilitation

		FY 2005 Performance*	FY 2003 - FY 2005 Cumulative Performance**
1	Loans and investments supporting real estate development and rehabilitation in low-income communities.	\$1.488 billion 361 loans/investments	\$2.328 billion 540 loans/investments
2	Square footage of commercial real estate projected to be developed and rehabilitated.	25 million square feet	43 million square feet
3	Number of full-time equivalent (FTE) construction jobs projected to be created.	38,420 FTEs	72,012 FTEs

QALICB: Business Support ***

1	Loans and investments supporting businesses operating in low-income communities.	\$451 million 549 loans/investments	\$729 million 307 loans/investments
2	Number of full-time equivalent (FTE) jobs created or maintained.****	8,552 FTEs	20,778 FTEs

CDE

1	Loans and investment in other CDEs.	\$10 million 4 loans/investments	\$27 million 11 loans/investments
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Loan Purchases

1	Purchase of loans from CDEs.	\$51 million	\$70 million
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FCOS

1	Investment in Financial Counseling and Other Services (FCOS).	\$105 thousand	\$250 thousand
2	Number of businesses receiving FCOS.	316 businesses served	523 businesses served

* Fiscal Year (FY) 2005 performance is based on data available as of September 6, 2006. At that time, the Fund had not completed the "cleansing" process for CIIS data. During cleansing, the Fund reviews the data for consistency and general logic. The data in the table represent 60 cleansed and 43 uncleansed CIIS reports. Of the 103 CDEs that reported in FY 2005, 94 provided a TLR, and of these, 84 reported providing new loans or investments in QALICBs in FY 2005.

** Cumulative performance is based on data available as of September 6, 2006. Each year, allocatees are permitted to update data reported in previous fiscal years to correct errors or provide newly available information. As a result, the cumulative figures may not exactly add up to the FY 2003, FY 2004, and FY 2005 annual performance figures reported by the Fund in this and previous Performance and Accountability reports.

*** Business Support includes loans and investments with a purpose of "Other," which includes, for example, equity investments in operating businesses.

**** The FY 2005 jobs figure includes jobs created in FY 2005 by businesses financed in prior years as well as businesses financed in FY 2005.

OVERVIEW OF THE BANK ENTERPRISE AWARDS PROGRAM

The Bank Enterprise Award (BEA) Program recognizes the key role played by traditional financial institutions in community development lending and investing. It provides incentives for regulated banks and thrifts to invest in CDFIs and to increase their lending and financial services in economically distressed communities. Providing monetary awards for community reinvestment leverages the Fund's dollars and puts more capital to work in distressed communities throughout the nation. By statute, the BEA Program is highly targeted to areas with larger populations. In general, approximately 4000 Census Tracts qualify as "distressed communities" under the program.

BEA Program awards are based on a percentage of the increase in the amount of Qualifying Activities from a Baseline Period to a later Assessment Period (the corresponding time the following year). Qualified Activities consist primarily of financial assistance provided to certified CDFIs as well as the various loans made by financial institutions (for example, affordable housing loans, small business loans, real estate development loans), and services (such as access to automated teller machines and opening of savings accounts).

Promoting CDFI Investments Through the BEA Program

The BEA Program has a dual purpose. The first priority is to increase banks' financial support of CDFIs in order to build CDFI self-sufficiency and capacity (referred to as CDFI Related Activities). The second priority is to build the capacity of Federal Deposit Insurance Corporation (FDIC) insured depository institutions (banks) to expand their community development lending and investments within severely underserved areas (referred to as the Distressed Community Financing Activities and Service Activities).

By statute, the Fund must award applicants in the CDFI Related priority before making awards to applicants in the Financing Activities priority and Service Activities priority.

The prospect of a BEA Program award encourages banks to achieve this first priority by providing low cost capital and operating support to CDFIs, which has helped to create and sustain a network of CDFIs. CDFIs serve as a delivery mechanism for banks to partner with to better serve highly distressed neighborhoods.

Eligibility

All depository institutions insured by the FDIC are eligible to apply for a BEA Program award. The BEA Program rewards actual increases in the dollar volume of Qualified Activities from a Baseline Period to a later Assessment Period. Qualified Activities for the BEA Program are divided into three priority areas:

1. **CDFI-Related Activities:** Equity investments (grants, stock purchases, purchases of partnership interests or limited liability company membership interests), equity-like loans, and CDFI support (loans, deposits or technical assistance) to certified CDFIs (referred to as CDFI Partners).
2. **Distressed Community Financing Activities:** Loans or investments for affordable home mortgages, affordable housing development, education, small businesses, and commercial real estate development in economically distressed communities.
3. **Service Activities:** Deposits, financial services (such as check-cashing, money orders, or certified checks), electronic transfer accounts (ETAs), individual development accounts (IDAs), First Accounts, or community services provided to low-to moderate-income individuals or the institutions serving them.

Changes to the BEA Program During FY 2006

There were no substantive changes to the BEA Program in FY 2006.

FY 2006 BEA Program Awards

For FY 2006, the Fund received 59 eligible applications requesting just over \$45 million, compared to 84 applications requesting almost \$49 million in the prior year. The Fund selected 47 FDIC-insured institutions to receive just under \$12 million in awards. The FY 2006 applicants are headquartered in 15 states, compared to the 33 states represented the prior year.

FY 2006 applicants provided \$368 million in loans or investments in distressed communities, \$72 million in loans, deposits and technical assistance to CDFIs, and \$2 million in equity investments and grants to CDFIs.

FY 2006 Community Impact

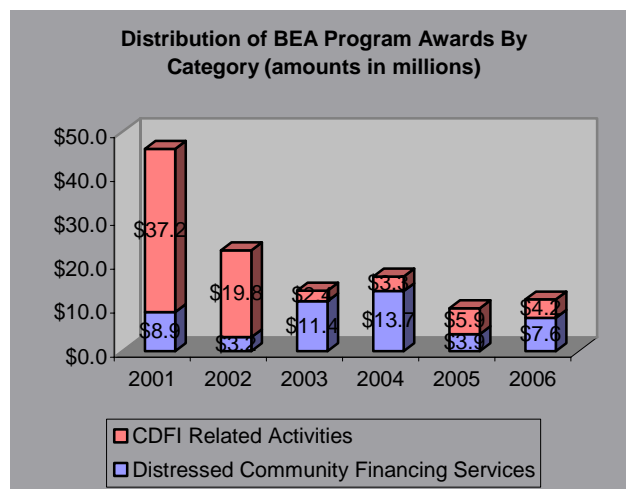
The 59 FY 2006 eligible applicants increased their qualified community development activities by \$318 million over the prior year.

- \$245 million increase in loans and investments in distressed communities;

- \$70 million increase in loans, deposits, and TA to CDFIs;
- \$2 million increase in equity investments or grants; and
- \$1 million increase in financial services in distressed communities.

BEA Program Awardee Activities

The trend of investments in distressed communities and investments in CDFIs by BEA awardees is shown in the Distribution of BEA Program Awards by Category chart.



OVERVIEW OF NATIVE INITIATIVES

The CDFI Fund's Native Initiatives originated from the findings of the CDFI Fund's "Report on the Native American Lending Study" (the Lending Study), which was delivered to Congress in November 2001. The study of access to capital in Native American, Alaska Native and Native Hawaiian communities (collectively referred to as Native Communities) identified barriers to private financing on such lands, identified the impact of such barriers on access to capital and credit for Native Communities, and suggested remedies that the CDFI Fund could implement to address them.

The Fund's Native Initiatives are about expanding native opportunity by overcoming barriers that prevent access to credit, capital and financial services in Native Communities through the creation and expansion of CDFIs primarily serving Native Communities (referred to as Native CDFIs). Thus, the dual focus of the Native Initiatives is to assist Native Communities and Native organizations to create Native CDFIs as well as to strengthen the operational capacity of existing Native CDFIs.

The Native Initiatives are based on six objectives:

1. Expand training opportunities in community development finance for Native Communities;
2. Offer Technical Assistance to overcome barriers to the creation or sustainability of Native CDFIs;
3. Offer technical and Financial Assistance awards targeted to meet the needs of existing or proposed Native CDFIs;
4. Encourage traditional financial institutions to increase their provision of financial products and services in Native Communities;
5. Support the provision of financial education to Native Communities; and
6. Facilitate networking and in-depth training forums in community development finance.

Components of Native Initiatives

The Native Initiatives work to achieve the above six objectives through two principle strategies: a funding program – the Native American CDFI Assistance (NACA) Program – targeted to increasing the number and capacity of existing or new Native CDFIs, and a complementary training initiative that seeks to foster

the development of new Native CDFIs and to strengthen the operational capacity of existing Native CDFIs.

NACA Program

The NACA – Native American CDFI Assistance - Program supports Native CDFIs and entities proposing to become Native CDFIs, to help build their capacity to better address the community development and capital access needs of Native communities. The NACA Program was introduced in FY 2004 to expand on and consolidate our previous NACD and NATA funding programs. The NACA Program provides Financial Assistance (FA) and Technical Assistance (TA) grants to Native CDFIs (replacing formerly funded TA through NATA); and TA grants to entities proposing to become or create Native CDFIs (formerly funded through NACD).

In FY 2006, the Fund received 39 NACA applications requesting nearly \$14 million, including twelve requests for \$8.4 million in FA. The Fund awarded a total of \$4.2 million to 21 organizations, compared to 22 awards totaling \$3.5 million during the prior year.

Financial Assistance (FA) Grants

Under the NACA Program, eligible Native CDFIs may receive FA awards (such as loans or grants depending on the source of matching funds) to support their financing activities. The Fund made six FA awards in the FY 2006 funding round totaling \$2.25 million (five of the organizations also received TA grants totaling \$519,000), compared to four FA awards totaling \$1.3 million made in FY 2005 (these same four awardees also received \$540,000 in TA grants).

Technical Assistance (TA) Grants

The NACA Program provides TA grants for capacity building uses, including operating grants for start-up Native CDFIs and Native organizations seeking to create a Native CDFI. Awardees may use TA grants

to acquire prescribed types of products or services including technology (usually computer hardware and

software), staff and board training, consulting services to acquire needed skills or services (such as a market analysis or lending policies and procedures), staff time to conduct discrete, capacity-building activities (such as website development), and for certain applicants -- general, ongoing, operational activities (such as general staff salary, rent and utilities, etc.).

In FY 2006, the Fund awarded \$2.0 million in TA grants to 20 organizations through the NACA program, compared to \$2.1 million provided to 22 organizations during the prior year.

Training Initiatives

Native Communities Financing Initiative

The CDFI Fund contracts for the provision of training and technical assistance to Native lenders, financiers, and community development practitioners interested in developing Native CDFIs through the Native Communities Financing Initiative (NCFI). The NCFI is an intensive series of workshops conducted over 12 months to help Native communities develop and grow Native CDFIs. In 2006, over 44 participants from 26 Native communities participated in an NCFI workshop. Since 2003, nearly 235 Native communities and organizations have participated in a workshop.

New in 2006, the CDFI Fund expanded the NCFI training to provide TA to ongoing CDFIs. During the first half of 2006, this training included nearly 180 days of TA. The Fund also launched more Financial Education Train-the-Trainer events and a new Native Credit Union training.

Native IDA Initiative

In November 2004, the CDFI Fund awarded the Native Individual Development Account (IDA) Initiative contract. The contractor provides training and TA to help Native CDFIs and other Native groups establish, implement, and sustain IDAs as a strategy to increase demand for Native CDFI financial products and services.

The Native IDA Initiative will sponsor a total of eight regional institutes through 2007. Regional institutes in

2006 included 88 participants in 3 locations: New Mexico, Minnesota, and Alaska. A fourth institute will be completed in Florida in November 2006 and additional institutes in Hawaii, Colorado, and Washington D.C. during 2007. Each training is open to ten organizations (e.g., a Native CDFI, a tribe, or a Native organization) and is paired with follow-on TA. Groups participating in the New Mexico, Minnesota, and Alaska institutes received 188 cumulative hours of follow-on TA during 2006.

Announcement of New Contracts

Under a new program sponsored by the CDFI Fund's Expanding Native Opportunities Initiative, First Nations Oweesta Corporation (Oweesta) has been contracted to deliver four, three-day financial education workshops based on the ***Building Native Communities*** financial education series tailored to a Native CDFI audience. Accompanying this training will be up to six days of technical assistance per attending group to help them develop financial education programs for their communities. These CDFI Fund sponsored trainings will provide Native CDFIs with the tools and guidance to engage other community organizations to build an effective program that is user friendly to all age groups.

Also part of the contract, Oweesta will partner with ONABEN and CFED to develop a Native focused national entrepreneurship curriculum and training and technical assistance program that builds on current local efforts, captures effective practices, and encourages sustainable and collaborative models. As part of this program, Oweesta and its partners will examine the potential of integrating existing entrepreneurship curricula, including CFED's *Rural Entrepreneurship through Action Learning (REAL)* curricula and ONABEN's *Indianpreneurship: A Native American Journey into Business* to produce a Native Entrepreneurship Education Curriculum and Facilitators Implementation Manual for use at a Native Entrepreneurship Facilitator's Institute.

Participating Native CDFIs and other organizations, such as tribal colleges, will learn how to incorporate experiential entrepreneurship education into their development services programming. Participants will interact with experienced entrepreneurship education facilitators, prepare lesson and course plans, and experience the highlights of the entrepreneurship

education curricula as their own students will. The individual follow-up technical assistance will focus on working with the organizations to help adapt the principles and curriculum to help integrate entrepreneurship in each organization's menu of services.

The CDFI Fund also awarded a contract to Opportunity Finance Network (OFN). This contract will extend the NCFI series of workshops and TA for one additional year to serve an additional round of Native participants. It will also extend TA for past participants of NCFI. Additionally, this contract will: 1) introduce two rounds of a training program targeted at Native credit union CDFIs; 2) develop an impact measurement tool for use by Native CDFIs; 3) introduce a peer shadow/mentoring program; and 4) provide TA for mature and existing Native CDFIs to enable these organizations to strengthen or increase the services they are able to offer.

FY 2006 Performance

The performance goal for the Native Initiatives is to build the capacity and coverage of CDFIs and other institutions to provide credit, capital, and related services to Native communities. The CDFI Fund tracks two corresponding annual performance measures: (1) the annual percentage increase in the number of Native CDFIs; and (2) the annual percentage increase in the total assets of Native CDFI awardees.

In FY 2006, the number of certified Native CDFIs increased from 36 to 39 entities. Between FY 2005 and FY 2006, Native awardees showed growth of 182% in assets, far exceeding the projected 33% growth.¹ The tremendous growth was driven by nearly every organization showing some growth and a single start-up CDFI that increased its assets more than ten-fold. Native CDFIs increased their total assets by 103 percent between FY 2004 and FY 2005. The Fund has a small number of Native CDFIs that report from year-to-year (six in FY 2005); therefore, the performance of a single CDFI can have a great impact on the average change in assets. In FY 2005, a single CDFI increased its total assets by 350 percent, leading to the 103 percent increase of the entire group.

¹ * As of the date this report was produced, the Fund had not completed the "cleansing" process for CIIS data. During cleansing, the Fund reviews the data for consistency with the CDFI's financial statements and overall reasonableness. The data in this table represent 5 cleansed and 2 uncleansed CIIS reports.

Status of Financial Management

STATUS OF FINANCIAL MANAGEMENT

This section includes the assurance statement required under the Federal Managers' Financial Integrity Act, a summary of the results of the FY 2006 financial statement audit, a summary of the financial management initiatives of the Fund during FY 2006, and a discussion of the Fund's financial position and results of operations during the past fiscal year.

**Department of the Treasury
Community Development Financial
Institutions Fund
Annual Assurance Statement for FY 2006**

As the Director of the Community Development Financial Institutions Fund, I have established internal controls that enable me to provide reasonable assurance that laws and regulations are followed; programs achieve their intended results free from waste and mismanagement; resources are used consistently with our overall mission; controls are sufficient to minimize any improper or erroneous payments, and systems security is in substantial compliance with all relevant requirements. Furthermore, continuity of operations planning in critical areas is sufficient to reduce risk to a reasonable level. With the exception of certain performance information that is provided by program awardees, performance data is reliable. I base my assurance on internal evaluations, management assessments and the results of our prior and current year financial statement audits. Also, I can provide reasonable assurance that the objectives of Sections 2 and 4 of the Federal Managers' Financial Integrity Act were achieved.

In addition, the Fund substantially complies with the requirements of the Federal Financial Management Improvement Act. The Fund's financial management systems substantially comply with the federal financial management systems requirements, applicable accounting standards, and use the United States Standard General Ledger at the transaction level.



**Arthur Garcia,
Director**

Description of the CDFI Fund's Financial Management System

The Fund contracts for accounting services under a franchise agreement with the Bureau of the Public Debt's Administrative Resource Center (ARC) in Parkersburg, West Virginia. While the ARC maintains the accounting system relating to the Fund's transactions, the Fund is responsible for generation of all source documents and the accuracy of all accounting information.

The Fund's financial management system includes the transactions maintained by ARC in the accounting system as well as records maintained and procedures performed by the Fund's financial management staff in Washington, D.C. The Fund's financial management staff is directly responsible for the administrative control of its funds, financial planning, budget formulation and execution, and review and analysis of financial information.

Results of FY 2006 Financial Statement Audit

FY 2006 marks the eighth consecutive year in which the auditors rendered an unqualified opinion on the Fund's financial statements and in which no material weaknesses were identified. The auditors identified one instance of non-compliance with laws and regulations and two reportable conditions. The non-compliance issue pertained to the Fund's lack of a process to ensure that Single Audit Act annual reports required from awardees are received in a timely manner, pursuant to OMB Circular A-133. These reports are used to monitor awardee compliance with the terms of their assistance agreements.

The two reportable conditions were as follows:

1. The Fund needs to identify on a more timely basis costs capitalized as internal-use software in development that:

- Will not result in a software module. Accumulation of such costs needs to end, and the accumulated costs are to be written off at the time that this determination is made; and
- Have resulted in a software module previously placed in service. Such costs should have been transferred to an internal-use software asset account and amortized in the period the related module was placed in service.

For both of the above situations, the Fund made the related determinations well after the related fiscal years in which such determinations should have been made. The Fund will address this recommendation by having periodic meetings between the appropriate financial and system managers to review the status of software projects.

2. The Fund does not have an adequate process in place to monitor the timely receipt of annual information from awardees to monitor their compliance with the terms of their assistance agreements. The Fund has not yet determined how it will address this finding.

FY 2006 Financial Management Initiatives

In FY 2006, the financial management focus was one of continuing to implement and enhance initiatives begun in prior years. Implementation of and enhancements to the Community Investment Impact System as discussed below was a priority of the Fund as well as enhancements to other Fund systems.

Community Investment Impact System (CIIS)

CIIS is a web-based system designed to collect an Institution Level Report (ILR) and Transaction Level Report (TLR) from CDFIs and CDEs. The CDFI CIIS data collected includes the organization's profile, financial position, portfolio, community impacts, development services, other products and services, and compliance measures. The CDE CIIS data collected includes the organization's profile, QEI distribution, portfolio, loan purchases, and financial counseling and

other services.

In fiscal year 2006, CIIS was used by 276 CDFIs and 114 CDEs. Fiscal year 2006 showed a tremendous increase in transaction level data being reported as 160 organizations submitted the details of nearly 20,000 loans and equity investments. This is more than double the number of transactions reported in the previous year. The Fund intends to use the transaction level data to demonstrate the impact CDFIs and CDEs have in local communities, to educate the public about community development finance, and to compare CDFI and CDE portfolios over time. In addition, the Fund is preparing to make the CIIS data available to the public within the parameters of all applicable Federal information protection, privacy and confidentiality laws.

The Fund also made major enhancements and changes to its CIIS database, which serves as a repository for the data collected through the CIIS data collection system. The changes are structural in nature and allow for more efficient storage and retrieval of the data as well as maintaining compatibility with prior year data collections. Additionally, the Fund has purchased and installed a commercially available software tool called SAS to enhance and improve performance of statistical analysis and reporting on the CIIS data.

Much of the performance information in The Community Development Financial Institutions Program section of the Discussion and Analysis section was provided by an analysis of CIIS data.

Migration to Grants.gov for Paperless Processing of Applications

The Federal Financial Assistance Management Improvement Act (P.L. 106-107), and the President's Management Agenda require all federal grant making agencies to completely migrate their electronic program applications to the Grants.gov system administered by the Department of Health and Human Services by FY 2007. During FY 2006, the Fund abandoned use of its own electronic applications system and migrated the Financial Assistance, Technical Assistance, and Bank Enterprise Award program applications to the Grants.gov system. Although the technical aspects of the migration were successful, transition to the new system for our applicants proved a bit more challenging. The

Grants.gov registration process is significantly more involved than the Fund's process and takes several days to complete. Despite an aggressive outreach campaign conducted by the Fund, many of our applicants still encountered unanticipated problems in completing and submitting their applications.

Migration to a Grants Management Line of Business for Internal Application Processing

The Federal Financial Assistance Management Improvement Act and the President's Management Agenda also require that all federal grant making agencies completely migrate their electronic grant processing systems to one of three federally selected centers of excellence. This initiative is known as the "Grants Management Line of Business". CDFI is at the forefront of this initiative by having already selected the Department of Health and Human Services, Administration for Children and Families, as our grant processor. Planning for the transition began in FY 2006 and the entire transition is expected to last through FY 2009. During the transition period, the Fund will continue to run parallel systems for seamless operations and there will be no disruption of services to our customers.

CDFI Fund Web Site

The CDFI Fund web site underwent two significant changes in FY 2006. First, as a cost savings measure, the web site was transitioned from a commercial web hosting service provider to a federally owned franchising service. This transition was completed successfully and with minimal disruption of service to our customers. This transition resulted in a significant annual cost savings to the government. Second, the web site was updated with a new layout to make it easier for our customers to locate the information they are looking for.

MyCDFIFund

The Fund's myCDFIFund web based portal is not affected by the migration of our electronic applications to Grants.gov or the Grants Management Line of Business. We continued to use this portal throughout FY 2006 to allow customers to map target markets, update their personal information, and retrieve award

information. The system was enhanced to include the full electronic submission of all CDFI and CDE certification applications (not affected by Grants.gov) including an automated "signature page" and an upload feature for the application.

Customer Information Mapping System (CIMS)

The Fund's Customer Information Mapping System (CIMS) is not affected by the migration of our electronic applications to Grants.gov or the Grants Management Line of Business. We continued to maintain and improve CIMS throughout FY 2006. The system was enhanced to allow the submission of target market maps along with Certification applications and to supplement CDFI Fund program applications (a feature not available on the Grants.gov system).

Management Responsibilities

Fund management is responsible for the fair presentation of information contained in the principal financial statements in conformity with accounting principles generally accepted in the United States of America. Management is also responsible for the fair presentation of the Fund's performance measures in accordance with the Office of Management and Budget requirements. The quality of the Fund's internal control structure rests with management, as does the responsibility for identification of and compliance with applicable laws and regulations.

Limitations of the Financial Statements

The financial statements report the financial position and results of operations of the Community Development Financial Institutions Fund for the years ended September 30, 2006 and 2005, pursuant to the requirements of 31 U.S.C. 3515(b). While the statements have been prepared from the books and records of the Fund in conformity with accounting principles generally accepted in the United States of America, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Analysis of Financial Position and Results of Operations

Summarized Financial Data (amounts in millions)			
	FY 2006	FY 2005	Increase / (Decrease)
Assets	\$146.5	\$159.9	(\$13.4)
Liabilities	\$52.0	\$52.4	(\$0.4)
Net Position	\$94.5	\$107.5	(\$13.0)
Revenue and Financing Sources	\$59.7	\$71.9	(\$12.2)
Expenses	\$64.9	\$72.8	(\$7.9)
(Shortage) of Revenue and Financing Financing Sources Under Expenses	(\$5.2)	(\$0.9)	(\$4.3)

Assets

Assets decreased by \$13.4 million during the year, consisting primarily of a \$12.6 million decrease in Fund Balance with Treasury. Net loans receivable increased by \$3.5 million; other assets decreased by \$2.3 million; and net investments decreased by \$1.9 million.

Fund Balance with Treasury

Any change in Fund Balance with Treasury during the year results from the difference between the amount of appropriated funds received during the year (including amounts borrowed) and the amount expended.

The Fund Balance with Treasury increased gradually through FY 2001, and (with the exception of FY 2004) has decreased each year thereafter.

This annual decrease is the result of efforts undertaken starting in FY 2002 to reduce the amount of undisbursed awards, coupled with a reduction in amounts appropriated over the past several years.

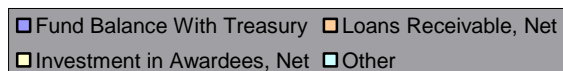
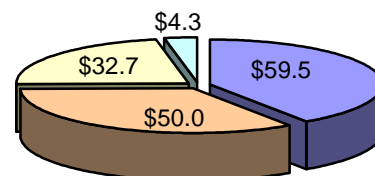
This decrease in undisbursed awards is largely the result of requiring a certain percentage of matching funds to be either in-hand or committed at the time of application submission. Once the related assistance agreements are signed by the Fund and the awardee, a disbursement can be made almost immediately rather than waiting for the matching funds to be obtained.

The decrease in the Fund Balance with Treasury is also a function of the amount of the annual appropriation received from Congress. Since the annual appropriation received has decreased each year since FY 2001 (receipt of the annual appropriation increases the Fund Balance with Treasury) it takes a smaller amount of annual award disbursements to have a greater reduction in the fund balance. We anticipate the Fund Balance with Treasury to decrease into the foreseeable future.

Loans Receivable

Loans receivable are increased when CDFI Program loan awards are disbursed by the Fund. The \$3.5 million net increase in loans represents the difference between loan awards disbursed and collected during the year (\$7.0 million and \$2.4 million, respectively), less the related increase in the allowance for bad debts of \$1.1 million (the allowance is equal to 25 percent of the amount of loans).

Allocation of Fund Assets
September 30, 2006
(amounts in millions)



Liabilities

The decrease in liabilities during the year of \$.4 million consisted of a decrease in awards payable of \$.3 million offset by an increase in debt of \$.4 million. Awards payable consists primarily of undisbursed BEA awards (recorded as a liability at the time of award) and a smaller amount of CDFI Program award disbursements approved at year-end but not processed.

Awards Payable

Awards payable have decreased every year since 2001 for two reasons: 1) the Fund's annual budget appropriations peaked in FY 2001 and have decreased each subsequent year; so there is a smaller amount of BEA Program awards to make each year, and 2) the Fund has been able to disburse a significant amount of BEA awards over the past several years, since there is no matching funds requirement for BEA awardees. Although the Fund made an additional \$12.0 million in new BEA awards during the year, total disbursements (and deobligations) of BEA awards were \$15.5 million, resulting in a net decrease in BEA awards payable of \$3.5 million.

CDFI Program awards are accrued as liabilities to the extent that award disbursements have been approved at year-end but not disbursed. There were no such liabilities at the end of FY 2006, which represented a reduction from the prior year of \$1.8 million.

Debt

The increase in debt of \$4.9 million relates to additional borrowings (net of repayments) necessary to fund loans made during the year to awardees, and to fund the downward subsidy reestimate. Awards made in the form of loans are funded in part by borrowings from Treasury.

For Federal budget purposes, the Fund is required to annually recompute the estimated amount of subsidy on prior loans made to awardees. This subsidy represents the difference between the present value of the projected future cash flows on loan awards and the face amount of the loans. It is based on historical payment information not available at the time of award, and on current interest rates. Accordingly, an upward or downward reestimate adjustment will be required every year. A downward adjustment means that prior subsidy estimates were overstated – amounts appropriated in prior years for loan subsidies were in excess of what was needed – and so the Fund borrows this amount to repay to the Treasury Department.

Net Position

Net position decreased during the year by \$13 million. Net position will change during the year as a result of

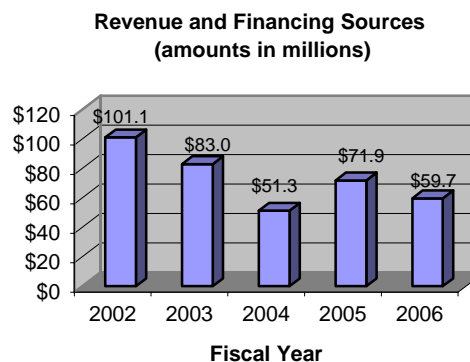
the following: 1) the difference between appropriations received (net of appropriations cancelled, rescinded and adjusted for credit subsidy re-estimates) and appropriations used; 2) any adjustment of the Fund's subsidy reestimate, and 3) the excess (or shortage) of revenue and financing sources over (under) expenses. During FY 2006, appropriations received (net of amounts cancelled and rescinded) were \$51.1 million, and appropriated capital used was \$57.4 million. This difference of \$6.3 million decreases net position.

During the year the Fund adjusted its subsidy reestimate downward by \$1.5 million, which required an additional borrowing from Treasury. As stated above, the amount borrowed is used to pay back to the Treasury Department the excess subsidy amounts appropriated in prior years. This \$1.5 million repayment reduces net position.

The shortage of net revenue and financial sources under expenses contributed an additional \$5.2 million of the decrease in net position (this amount is discussed below).

Revenue and Financing Sources, Expenses, and Shortage of Revenue and Financing Sources Under Expenses

Revenue and Financing Sources



The primary source of revenue and financing sources for the Fund is the annual appropriation ("appropriated capital used" as reflected in the statement of operations). Pursuant to Federal grant accounting requirements, the amount of appropriated funds recognized as revenue is, with certain adjustments,

equal to the amount of operating expenses for the year. Operating expenses for the year were \$60.6 million; however, \$4.3 million of this amount was funded from the no-year account (this amount pertains to CDFI grants), which is not part of the annual appropriation. Accordingly, appropriated capital used is equal to this net \$56.3 million amount, plus an additional \$1.1 million pertaining to additional expenses funded.

As stated above, appropriated funds are used to fund operating expenses, and so a change in operating expenses will generally explain the reason for the change in appropriated capital used. The reduction in operating expenses includes a reduction in award expenses of \$13.3 million. However, \$3.8 million of this reduction pertains to amounts funded from the no-year account and so do not use appropriated funds. Accordingly, the reduction in award expenses which is funded from appropriated funds is \$17.1 million (the \$13.3 million plus the \$3.8 million). This amount, offset by the increase in administrative expenses of \$4.1 million and by an additional decrease in appropriated capital used of \$.5 million (not detailed) is why appropriated capital used decreased from the prior year amount.

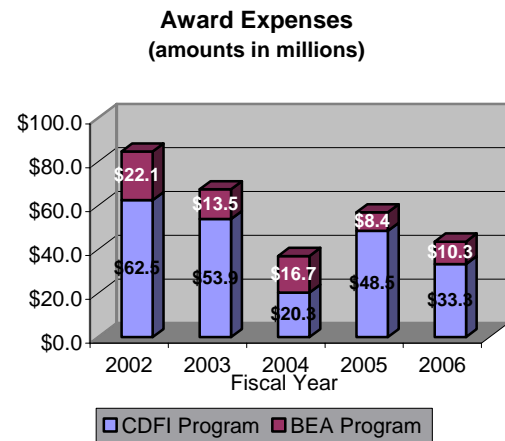
Expenses

The change in the Fund's operating expenses during FY 2006 consisted of the following:

Comparison of Operating Expenses Fiscal Years 2006 and 2005 (amounts in millions)			
	<u>FY 2006</u>	<u>FY 2005</u>	<u>Difference</u>
Award Expenses	\$43.6	\$56.9	(\$13.3)
Administrative Expenses	\$15.9	\$11.8	\$4.1
Bad Debt Expense	\$1.1	\$1.3	(\$0.2)
Total Operating Expenses	<u>\$60.6</u>	<u>\$70.0</u>	<u>(\$9.4)</u>

Award Expenses

The decrease in award expenses of \$13.3 million during the year consisted of a decrease in CDFI grant expense of \$15.2 million offset by an increase in BEA grant expense of \$2 million.



Under the BEA Program, awards are recognized as expenses at the time a notice of award is signed by the Fund. Accordingly, the FY 2006 BEA Program expense was larger than the prior year due to a larger amount of awards being made during the year (the BEA Program expense during the year will not equal the amount of awards made due to deobligations in the current year of prior year awards, which are accounted as a reduction to the current year expense). This is due to a decrease in the amount of funds appropriated for the year by Congress for the BEA Program.

Under the CDFI Program, awards pertaining to grants are recognized as an expense at the time award disbursements are made (reduced by current year deobligations or prior year awards), while awards pertaining to loans and equity are treated as increases to loans receivable and investments, respectively, at the time of disbursement.

CDFI Program expenses decreased during the year due to a decrease in the amount of CDFI Program grant disbursements being made as compared to the prior year.

As can be seen in the accompanying chart, while there was a significant reduction in the amount of CDFI grants disbursed (and therefore expensed) during FY 2006, the amount disbursed as a percentage of the beginning undisbursed balance was higher than the prior year.

**Relationship Between CDFI Program
Grant Expense and Undisbursed Awards
(amounts in millions)**

	<u>FY 2006</u>	<u>FY 2005</u>
CDFI Program Grant Disbursed	\$33.3	\$47.7
Beginning Balance of Undisbursed Awards	\$39.0	\$60.7
Percentage of Beginning Balance Disbursed	<u>85.4%</u>	<u>78.6%</u>

Administrative Expenses

During FY 2006, the Fund determined that \$2.5 million amount of software costs carried as assets on the prior year's balance sheet as "software costs in development" had no future benefit and so were written off (this write-off is included in administrative expenses). The remaining amount of these software costs in development as of September 30, 2005 were deemed to have either been placed in service during a prior period, or pertained to projects completed during FY 2006. For those software projects completed in a prior period, the related amortization cost pertaining to these prior periods of \$172 thousand is included in current year administrative expenses. All other software costs incurred during FY 2006 that did not pertain to software projects placed in service during the year were expensed as maintenance expenses; this amount totaled \$725 thousand. There was no software-in-development as of September 30, 2006, and so software maintenance expense was significantly higher in FY 2006 than in prior years; this is also part of the reason for the increase in administrative expenses.

Bad Debt Expense

Bad debt expense is a function of the amount of loans receivable at year-end. The Fund's allowance for bad debts is equal to 25 percent of loans receivable. The net increase in loans receivable during FY 2006 (the amount of CDFI Program loan awards disbursed in excess of loan repayments) was \$4.6 million, resulting in an increase to the allowance for bad debts of \$1.1 million.

Shortage of Revenue and Financing Sources Under Expenses

As stated above, the amount of appropriated capital used (the largest component of the Fund's revenue) is, with certain adjustments, equal to the amount of operating expenses for the year. Accordingly, the shortage of revenue and other financing sources over expenses (the Fund's "net loss") will consist of the amount by which expenses not covered by budgetary resources exceeds revenue and financial sources other than appropriated capital used.

For FY 2005, expenses not covered by budgetary resources totaled \$7.1 million, consisting of interest expense on Treasury borrowings of \$2.8 million and \$4.3 million of grants and loan subsidy disbursed from the Fund's no-year account. The no-year account is a non-appropriated account consisting of interest income, dividend income and proceeds from the redemption of equity investments, accumulated since Fund inception.

Revenue and financial sources other than appropriated capital used totaled \$1.9 million consisting of interest and dividends of \$1.8 million and a \$.1 million realized gain on the disposition of investments. The excess of the \$7.1 million of expenses not covered by appropriations exceeds the \$1.9 million of revenue and financing sources other than appropriated capital by \$5.2 million, representing the shortage of revenue and financing sources under expenses.

Independent Auditors' Reports



KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report

Inspector General, U.S. Department of the Treasury, and the
Director, Community Development Financial Institutions Fund:

We have audited the accompanying statements of financial position of the U.S. Department of the Treasury's Community Development Financial Institutions Fund (the Fund) as of September 30, 2006 and 2005, and the related statements of operations and changes in net position and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the applicable provisions of Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Department of the Treasury's Community Development Financial Institutions Fund as of September 30, 2006 and 2005, and its operations and changes in net position and cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The information in the Program's Discussion and Analysis section is presented for the purpose of additional analysis and is not a required part of the financial statements. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The information in the Community Development Financial Institutions Fund Overview and the information in the appendices are presented for purposes of additional analysis and are not required as part of the financial statements. This information has not been subjected to auditing procedures and, accordingly, we express no opinion on it.



In accordance with *Government Auditing Standards*, we have also issued our reports dated November 8, 2006, on our consideration of the Fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audits.

KPMG LLP

November 8, 2006



KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report on Internal Controls

Inspector General, U.S. Department of the Treasury, and the
Director, Community Development Financial Institutions Fund:

We have audited the statements of financial position of the U.S. Department of the Treasury's Community Development Financial Institutions Fund (the Fund) as of September 30, 2006 and 2005, and the related statements of operations and changes in net position and cash flows for the years then ended, and have issued our report thereon dated November 8, 2006.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the applicable provisions of Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of the Fund is responsible for establishing and maintaining effective internal control. In planning and performing our fiscal year 2006 audit, we considered the Fund's internal control over financial reporting by obtaining an understanding of the Fund's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 06-03. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audit was not to provide an opinion on the Fund's internal control over financial reporting. Consequently, we do not provide an opinion thereon.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Fund's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.



In our fiscal year 2006 audit, we noted certain matters, discussed below, involving the internal control over financial reporting and its operation that we consider to be reportable conditions. However, none of the reportable conditions are believed to be material weaknesses.

Software-in-Development

In performing procedures over the Software-in-Development asset account, we noted that CDFI Fund management:

- had capitalized maintenance costs of \$2.5 million that per SOP 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, should be expensed when incurred;
- had not transferred completed projects of \$538 thousand from the “in-development” account to the capitalized software account at the time such projects were considered completed; and
- had not recognized the \$172 thousand of amortization costs of these projects over their estimated useful life.

Had there been a process in place whereby the Fund Manager and Chief Information Officer (CIO) met on an ongoing basis to discuss software costs, the above issue could have been identified.

Recommendations

We recommend that the Fund Manager and CIO (or their designees) meet at least quarterly to discuss the status of costs incurred for the Software-in-Development account, including identifying when such costs will result in a completed software module to be placed in service. The meetings should also discuss any prior software costs to ensure that the dates such costs are to be placed in service are still valid.

Management’s Response

Management generally concurs with the finding and recommendation.

Grants Monitoring

Our audit revealed that even though the Fund has a system of awards management over its pre-award and award phases, the Fund has not developed sufficient procedures to determine if grant funds have been spent in accordance with their award agreements when awardees fail to submit annual information, including Single Audit reports. Specifically, while the Fund has a process in place which requires the submission of annual information, including Single Audit reports, used to monitor awardees compliance with the terms of their assistance awards, it does not adequately monitor the receipt of this information. Accordingly, this could result in awardees’ using Federal funds inconsistent with the objectives of the grant; programs and resources may not be protected from waste, fraud, and mismanagement; laws and regulations may not be followed; excess funds not spent may not be returned; and reliable and timely information may not be obtained, maintained, reported, or used for decision-making.

Recommendations

We recommend that the Fund improve post-award monitoring, which will help ensure compliance with the requirements of *Single Audit Act Amendments of 1996*, by:



- developing a policy where sanctions are applied to awardees past due in submitting any component of their annual information, including Single Audit reports, in order to comply with OMB Circular A-133, and
- increasing the resources dedicated to post-award monitoring; this should include increasing the number of professionals fully focused on post-award monitoring and performing more desk reviews of information from the grantees on how the funds received were utilized and to recover unused granted funds, as necessary.

Management's Response

Management generally concurs with the finding and recommendation.

INTERNAL CONTROLS OVER PERFORMANCE MEASURES

Under OMB Bulletin 06-03, the definition of material weaknesses is extended to other controls as follows. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud, in amounts that would be material in relation to a performance measure or aggregation of related performance measures, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.

Our consideration of the internal control over the design and operation of internal control over the existence and completeness assertions related to key performance measures would not necessarily disclose all matters involving the internal control and its operation related to the design and operation of the internal control over the existence and completeness assertions related to key performance measures that might be reportable conditions.

As required by OMB Bulletin No. 06-03 in our fiscal year 2006 audit, with respect to internal control related to performance measures determined by management to be key and reported in the Program Discussion and Analysis, we obtained an understanding of the design of internal controls relating to the existence and completeness assertions and determined whether these internal controls had been placed in operation. We limited our testing to those controls necessary to test and report on the internal control over key performance measures in accordance with OMB Bulletin 06-03. However, our procedures were not designed to provide an opinion on internal control over reported performance measures and, accordingly, we do not provide an opinion thereon. In our fiscal year 2006 audit, we noted no matters involving the design and operation of the internal control over the existence and completeness assertions related to key performance measures that we considered to be material weaknesses as defined above.

We noted certain matters that we reported to the management of the Fund in a separate letter dated November 8, 2006.

* * *

This report is intended solely for the information and use of the Fund's management, the U.S. Department of the Treasury's Office of Inspector General, the OMB, the U.S. Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 8, 2006



KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report on Compliance and Other Matters

Inspector General, U.S. Department of the Treasury, and the
Director, Community Development Financial Institutions Fund:

We have audited the statements of financial position of the U.S. Department of the Treasury's Community Development Financial Institutions Fund (the Fund) as of September 30, 2006 and 2005, and the related statements of operations and changes in net position and cash flows for the years then ended, and have issued our report thereon dated November 8, 2006.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and applicable provisions of Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of the Fund is responsible for complying with laws, regulations, contracts, and grant agreements applicable to the Fund. As part of obtaining reasonable assurance about whether the Fund's financial statements are free of material misstatement, we performed tests of the Fund's compliance with certain provisions of laws, regulations, contracts, and grants agreements, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 06-03. Our audit procedures were not designed to test the requirements of OMB Bulletin No. 06-03 relating to the *Federal Financial Management Improvement Act* (FFMIA) of 1996, which are not considered applicable at the Fund level, but we did apply limited procedures to aid in the determination of compliance as part of the financial statement audit of the U.S. Department of the Treasury. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, contracts, and grants agreements applicable to the Fund. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests of compliance described in the preceding paragraph of this report disclosed one instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 06-03, and are described below.

Single Audit Act Amendments of 1996

The CDFI Fund does not have a policy to follow up on awardees that have failed to submit a Single Audit report as required under *Single Audit Act Amendments of 1996* (or submission of a "Single Audit exception letter," explaining why a Single Audit Report was not required).



In performing test work over the Fund's compliance with the monitoring requirements of *Single Audit Act Amendments of 1996*, we noted that 21 awardees failed to submit a Single Audit report or Single Audit exception letter, as required by OMB Circular A-133, and the Fund's requirements for awardees.

Recommendation

See the recommendation for Grant Monitoring in the Independent Auditors' Report on Internal Controls.

Management's Response

Management generally concurs with the finding and recommendation.

This report is intended solely for the information and use of the Fund's management, the U.S. Department of the Treasury's Office of Inspector General, the OMB, the U.S. Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 8, 2006

Financial Statements and Notes

Community Development Financial Institutions Fund
Statements of Financial Position
As of September 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Assets		
Current assets:		
Fund Balance with Treasury (Note 2)	\$ 59,458,807	72,077,789
Advances and prepayments	1,051,723	731,327
Loans receivable, net of allowance for bad debts of \$1,391,688 in 2006 and \$552,729 in 2005	4,175,063	1,658,188
Investments (Note 3)	100,000	-
Interest receivable	516,983	283,472
Total current assets	<u>65,302,576</u>	<u>74,750,776</u>
Long-term assets:		
Loans receivable, net of allowance for bad debts of \$15,283,024 in 2006 and \$14,974,652 in 2005	45,849,073	44,923,956
Investments, net of fair value adjustments of \$4,897,220 in 2006 and \$3,397,220 in 2005 (Note 3)	32,636,249	34,604,302
Internal-use software, net of accumulated amortization of \$1,636,593 in 2006 and \$924,262 in 2005	2,730,661	2,264,721
Internal-use software in development	<u>-</u>	<u>3,354,181</u>
Total long-term assets	<u>81,215,983</u>	<u>85,147,160</u>
Total assets	<u>\$ 146,518,559</u>	<u>159,897,936</u>
Liabilities and Net Position		
Current liabilities:		
Accounts payable	\$ 542,570	648,886
Awards payable	2,161,241	5,268,786
Accrued payroll	200,115	188,902
Accrued annual leave	267,404	245,608
Total current liabilities	<u>3,171,330</u>	<u>6,352,182</u>
Long-term liabilities:		
Debt (Note 4)	45,511,849	40,561,891
Awards Payable	3,295,705	5,451,128
Total long-term liabilities	<u>48,807,554</u>	<u>46,013,019</u>
Total liabilities	<u>51,978,884</u>	<u>52,365,201</u>
Commitments (Note 5)		
Net position (Note 6)	<u>94,539,675</u>	<u>107,532,735</u>
Total liabilities and net position	<u>\$ 146,518,559</u>	<u>159,897,936</u>

The accompanying notes are an integral part of these statements

Community Development Financial Institutions Fund
Statements of Operations and Changes in Net Position
Years Ended September 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Revenue and financing sources:		
Appropriated capital used	\$ 57,431,347	69,868,092
Imputed financing sources- expenses paid by others (Note 8)	478,247	345,759
Interest, non-federal	1,275,509	1,160,331
Interest, federal	248,342	293,930
Dividends	270,852	253,410
Total revenue and financing sources	<u>59,704,297</u>	<u>71,921,522</u>
Expenses:		
CDFI grants	33,287,740	48,495,565
BEA grants	10,337,645	8,374,171
Administrative (note 9)	15,433,520	11,448,138
Bad debt expense	1,147,331	1,360,574
Administrative expenses paid by others (Note 8)	478,247	345,759
Total operating expenses	60,684,483	70,024,207
Treasury borrowing interest	2,799,199	2,362,511
Unrealized loss on investments	1,500,000	647,220
Net Realized Losses (Gains) on Disposition of Investments	<u>(118,781)</u>	<u>(187,994)</u>
Total expenses	<u>64,864,901</u>	<u>72,845,944</u>
Shortage of revenue and financing sources under expenses (note 10)	\$ <u>(5,160,604)</u>	<u>(924,422)</u>
Changes in Net Position:		
Net position, beginning of year	\$ 107,532,735	125,157,025
Shortage of revenue and financing sources under expenses	(5,160,604)	(924,422)
Other changes (Note 7)	<u>(7,832,456)</u>	<u>(16,699,868)</u>
Net position, end of year	<u>\$ 94,539,675</u>	<u>107,532,735</u>

The accompanying notes are an integral part of these statements

Community Development Financial Institutions Fund
Statements of Cash Flows
Years Ended September 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Cash flows from operating activities:		
Shortage of revenue and financing sources under expenses	\$ (5,160,604)	(924,422)
Adjustments affecting cash flow:		
Appropriated capital used	(57,431,347)	(69,868,092)
Realized gain on disposition of investments	(118,781)	(187,994)
Unrealized loss on investments	1,500,000	647,220
Proceeds from disposition of investments	486,834	3,064,496
Amortization expense	712,331	455,569
Write-off of internal-use software in development	2,505,341	-
Interest on upward adjustment of prior year subsidy	-	(56,309)
(Increase) decrease in advances and prepayments	(320,397)	630,439
(Increase) in interest receivable	(233,512)	(114,990)
Increase in allowance for bad debts	1,147,331	1,360,574
Investments in awardees	-	(3,724,941)
Increase (decrease) in accounts payable and accrued payroll	(95,103)	164,347
Decrease in awards payable	(5,262,967)	(8,264,408)
Increase (decrease) in accrued annual leave	21,798	(24,738)
	<u>(62,249,076)</u>	<u>(76,843,249)</u>
Net cash used by operating activities		
Cash flows from investing activities:		
Acquisition of internal-use software	(329,433)	(1,069,806)
Loans disbursed	(6,957,528)	(7,808,648)
Collection of loan principal	2,368,206	2,366,354
	<u>(4,918,755)</u>	<u>(6,512,100)</u>
Net cash used by investing activities		
Cash flows from financing activities:		
Appropriations received	55,000,000	56,058,105
Appropriations cancelled	(3,363,017)	(1,891,505)
Appropriations rescinded	(550,000)	(444,176)
Borrowings from Treasury	7,574,474	6,347,451
Subsidy repayments to Treasury	(1,488,092)	(497,891)
Loan payments to Treasury	(2,624,516)	(3,008,090)
	<u>54,548,849</u>	<u>56,563,894</u>
Net cash provided by financing activities		
Net change in Fund balance with Treasury	(12,618,982)	(26,791,455)
Fund balance with Treasury, beginning of year	<u>72,077,789</u>	<u>98,869,244</u>
Fund balance with Treasury, end of year	<u>\$ 59,458,807</u>	<u>72,077,789</u>

The accompanying notes are an integral part of these statements

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

Notes to Financial Statements

September 30, 2006 and 2005

(1) Summary of Significant Accounting Policies

(a) *Reporting Entity*

The Community Development Financial Institutions Fund (the Fund) was created as a bipartisan initiative in the Riegle Community Development and Regulatory Improvement Act of 1994 (Public Law No. 103-325). The Fund was placed in the Department of the Treasury and began operations in July 1995.

The Fund operates various programs aimed at expanding the availability of credit, investment capital, and financial and other services in distressed urban, rural, and Native American communities. The Fund is intended to help create a national network of financial institutions dedicated to community development that leverages private resources (financial and human) to address community development needs.

The major programs operated by the Fund are the Community Development Financial Institutions Program (consisting of a Financial Assistance and Technical Assistance Component), the New Markets Tax Credit Program, the Bank Enterprise Awards Program, and Native American Initiatives.

The Community Development Financial Institutions (CDFI) Program provides financial and technical assistance awards to certified community development financial institutions (CDFIs) which in turn provide services to create community development impact in underserved markets. Financial assistance awards take the form of grants, direct loans, and equity investments. Technical Assistance grants provide assistance to start-up and early-stage CDFIs and entities planning to become CDFIs.

The Fund implemented the New Markets Tax Credit (NMTC) Program during fiscal year 2002. Under this program, the Fund provides an allocation of tax credits to Community Development Entities (CDEs), which use these credits to attract private sector investment. Proceeds from these investments are used for community development purposes. Unlike the Fund's grant programs, the allocation of tax credits to CDEs has no effect on the financial statements of the Fund.

The Bank Enterprise Awards (BEA) Program provides incentives to insured depository institutions (banks and thrifts) to invest in CDFIs and to increase their lending and financial services in distressed communities. Program participants are selected based on projected achievements. The awards are disbursed only after the activities have been implemented successfully, to ensure that only completed activities are recognized and that the Fund's limited dollars are effectively leveraged with private capital.

Through Native American Initiatives, the CDFI Fund provides grants to help create CDFI's and to build the capacity of existing Native CDFIs that serve primarily Native American, Alaska Native, and Native Hawaiian communities.

(b) *Basis of Presentation*

The American Institute of Certified Public Accountants (AICPA) has designated the Federal Accounting Standards Advisory Board (FASAB) as the standards-setting body for financial statements of federal

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

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governmental entities, with respect to the establishment of accounting principles generally accepted in the United States of America. FASAB has indicated that financial statements prepared based upon accounting standards published by the FASB may also be regarded as in accordance with generally accepted accounting principles for those federal entities, such as the Fund, that have issued financial statements based upon FASB accounting standards in the past. Accordingly, consistent with historical reporting, the Fund financial statements are presented in accordance with accounting standards published by the FASB.

Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation.

(c) *Fund Balance with Treasury*

The Fund does not maintain cash in commercial bank accounts. The U.S. Department of the Treasury (Treasury Department) processes cash receipts and disbursements. Fund Balance with Treasury is composed primarily of appropriated and borrowed funds (financing and program accounts) that are available to pay liabilities and finance authorized award and purchase commitments.

(d) *Fair Value of Financial Instruments*

The fair value of the Fund's financial instruments was determined as discussed below:

1) *Fund Balance with Treasury*

The carrying amount approximates fair value for Fund balance with Treasury because of the liquid nature of the funds with Treasury.

2) *Loans Receivable and Debt*

The carrying amount of loans receivable and debt approximates fair value because the related interest rates approximate current rates for similar loans and debt.

3) *Investments*

None of Fund's investments are in publicly traded entities for which a share price can be readily obtained; accordingly, the Fund estimated the fair value of investments as follows:

- Non-voting equity securities and limited partnership interest – Several factors were considered in estimating fair value for these investments, including, the cost of the investment, developments since the acquisition of the investment, the financial condition and operating results of the investee per their financial statements, the long-term potential of the business, recent share or unit prices paid, and other factors generally pertinent to the valuation of investments.

The Fund, in making its evaluation, has relied on financial data of awardees and, in many instances, on estimates by the management of the awardees as to the potential effect of future developments.

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- Convertible debt securities – Fair values were estimated using the same methodology as used for non-voting equity securities described above, based on the assumption that the securities were converted into stock.
- Secondary capital securities – These investments have terms similar to loans, and accordingly fair values were estimated by discounting future projected cash flows at the Treasury rate of securities with similar maturities.
- Certificates of deposit – The carrying amount approximates fair value because of the liquid nature of the investments.

4) Advances and Prepayments, Interest Receivable, Other Receivables, and Other Liabilities

The carrying amount of advances and prepayments, interest receivable, other receivables, and other liabilities approximate fair value as they represent the amounts expected to be realized or paid.

(e) Loans Receivable

The Fund provides assistance by making direct loans to certain CDFI Program awardees. Loans are reported as receivables when disbursed, reduced by a 25% default allowance. The Office of Management and Budget negotiated a 25% default allowance with the Fund to estimate future losses if adequate historical information is not available. Historical information is not available, and will not be available for some time due to the following: 1) the short length of time the loans have been outstanding; and 2) the majority of loans made by the Fund require either balloon payments at maturity, or principal payments commencing shortly before the maturity date. The borrowers, in accordance with the repayment schedules, have made timely interest and principal payments and there have not been any write-offs to date.

(f) Interest Receivable

Interest is accrued on the outstanding loans receivable principal balances and investments based on stated rates of interest.

(g) Investments

The Fund provides assistance to certain for-profit CDFI program awardees by purchasing non-voting equity and convertible debt securities and to Federal credit union awardees by purchasing certificates of deposit and by providing secondary deposits. Investments in CDFI program and Federal credit union awardees are stated at fair value.

In the event the Fund's evaluation results in an adjustment to fair value, an unrealized gain or loss is recorded and the investment balance is adjusted accordingly.

The Fund is restricted from owning more than 50% of the equity of awardees and from controlling their operations. The Fund considers convertible subordinated debentures to be equity investments because they exhibit sufficient characteristics of equity securities. For example, convertible subordinated debentures entitle the Fund to any dividends in the non-voting common stock into which it is convertible

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as if the Fund had converted the debentures into such stock prior to the declaration of the dividend.

(h) Internal-Use Software

Internal-use software represents the completed phases of various software placed in service during the year pertaining to 1) processing applications – this software automates the award application submission process; 2) geocoding – web-based software that geocodes addresses, map census tracts and counties, and enables applicants to determine the funding eligibility of census tracts and counties under CDFI's various programs; and 3) the Community Investment Impact System (CIIS) – a web-based data collection system for CDFI's and Community Development Entities.

The software is amortized using the straight-line method over the estimated useful life of seven years. Amortization expense for fiscal year 2006 and fiscal year 2005 was \$712,331 and \$455,569, respectively.

Internal-use software in development represents costs incurred for various software development projects not yet placed in service. During fiscal year 2006, the Fund determined that \$2.5 million of internal-use software in development as of September 30, 2005 was not going to have a future benefit, and so was charged off to operations with a corresponding recognition of appropriated capital used. There is no internal-use software in development as of September 30, 2006.

(i) Awards Payable

CDFI Program grant expense is recognized and awards payable are recorded when the fund is made aware, in writing, that the awardee has met the conditions required for payment and the Fund approves a grant disbursement to be made. BEA Program grant expense is recognized and awards payable are recorded when the Fund approves the BEA award to be made (i.e. at the time the funds are obligated).

The current and long-term portions of awards payable represent amounts estimated to be paid within the next twelve months (current portion) and thereafter (long-term portion) based on prior award payment experience.

(j) Retirement Plans

CDFI Fund employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). The FERS was established by the enactment of Public Law 99-335. Pursuant to this law, FERS and Social Security automatically cover most employees hired after December 31, 1983.

Employees hired prior to January 1, 1984, were provided an opportunity to join either FERS and Social Security or remain in CSRS.

All employees are eligible to contribute to the Thrift Savings Plan (TSP). For those employees participating in the FERS, a TSP account is automatically established, and the Fund makes a mandatory contribution of 1% of employee's base salary, to this account. In addition, the Fund makes matching contributions ranging from 1% to 4% for FERS eligible employees who contribute to their TSP account. Matching contributions are not made to the TSP accounts established by CSRS employees.

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FERS employees and certain CSRS reinstatement employees are eligible to participate in the Social Security program for retirement. In these instances, the Fund remits the employer's share of the required contribution. For CDFI Fund employees participating in CSRS, the Fund makes matching contributions to CSRS equal to 8.51% of base pay.

(k) *Annual, Sick and Other Leave*

Annual leave and compensatory leave is accrued as a liability when earned by the employee, and the accrual is reduced as leave is taken. The balance in this accrued liability account is computed using current pay rates. Sick leave and other types of non-vested leave are expensed as the leave is taken.

(l) *Debt*

Debt represents borrowings payable to the Treasury Department that were made to fund direct loans made by the CDFI Program. Principal repayments to the Treasury Department are required to be made based on the collections of loans receivable.

(m) *Contingencies*

The Fund may be a party in various administrative proceedings, legal actions, and claims brought by or against it. The Fund's management and legal counsel are unaware of any contingencies that would materially affect the Fund's financial position or results of operations.

(n) *Revenue and Financing Sources*

The Fund receives the majority of its funding through appropriations from the U.S. Congress. The Fund receives two-year appropriations that may be used, within statutory limits, for operating expenses. Appropriations are recognized as revenues at the time the Fund's grants are recorded as expenses, and when administrative expenses and provision for bad debts covered by budgetary resources are incurred.

Occasionally, the Fund receives dividends on its equity investments and may use those funds for operating expenses.

Additional revenue is obtained from interest received on direct loans to the public and on uninvested funds in the direct loan financing account held by the Treasury Department.

(o) *Tax Status*

The Fund, as a government entity, is not subject to federal, state, or local income taxes and, accordingly, no provision for income tax is recorded.

(p) *Use of Estimates*

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

Notes to Financial Statements

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(2) Fund Balance with Treasury

Fund balance with Treasury as of September 30, 2006 and 2005 consisted of the following components:

	<u>2006</u>	<u>2005</u>
Available	\$ 2,075,642	4,033,289
Obligated	54,798,076	64,393,783
Expired	<u>2,585,089</u>	<u>3,650,717</u>
	<u>\$ 59,458,807</u>	<u>72,077,789</u>

Fund balance with Treasury includes appropriated and borrowed funds available to pay liabilities and to finance authorized award and purchase commitments.

(3) Investments

Investments relate to capital provided to CDFI Program awardees. Investments consist of the following as of September 30, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Investments at Cost		
Non-voting equity securities	\$ 26,479,820	26,555,420
Convertible debt securities	2,573,882	2,573,882
Secondary capital securities	5,000,000	5,000,000
Limited partnership interest	3,354,767	3,647,220
Certificates of deposit	<u>225,000</u>	<u>225,000</u>
Investments at cost	37,633,469	38,001,522
Unrealized losses, net		
Non-voting equity securities	(4,000,000)	(2,500,000)
Limited partnership interest	<u>(897,220)</u>	<u>(897,220)</u>
Total unrealized losses, net	<u>(4,897,220)</u>	<u>(3,397,220)</u>
Investments at fair value	<u>\$ 32,736,249</u>	<u>34,604,302</u>

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

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September 30, 2006 and 2005

Non-voting equity securities consist of non-voting common stock held in for-profit CDFI Program awardees (preferred non-voting stock is held in two awardees).

Convertible debt securities consist of non-interest bearing convertible subordinated debentures. As of September 30, 2006 and 2005, one debenture of \$2 million matures January 2048 with the option to convert into 200,000 shares of non-voting class B common stock at a \$10 per share conversion price. The other debenture of \$573,882 as of September 30, 2006 and 2005, matures December 2013 with an option to convert to 1,434,706 shares of non-voting class E common stock.

The Limited Partnership interest consists of a Class B limited partnership interest in Sustainable Jobs Fund, LP, an interest in Pacific Community Ventures (acquired during fiscal year 2005), and three units of preferred interest in Shorebridge Capital LLC.

Secondary capital securities consist of investments that cannot be redeemed prior to scheduled redemption dates.

Certificates of deposits are investments in federal credit union awardees, and have interest rates ranging from 0 percent to 2 percent.

Investments included as current assets represent certificates of deposit that mature within the next twelve months.

(4) Debt

Debt consists of amounts borrowed from the U.S. Treasury Department and included the following activity for the years ended September 30, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Beginning balance	\$ 40,561,891	37,222,530
New borrowings	7,574,474	6,347,451
Repayments	<u>(2,624,516)</u>	<u>(3,008,090)</u>
Ending balance	<u>\$ 45,511,849</u>	<u>40,561,891</u>

The earliest principal repayment due date to Treasury is September 30, 2008. Principal payments on this debt as of September 30, 2006 are as follows:

2008	\$ 254,154
2009	1,793,981
2010	2,236,448
2011	92,920
2012	858,083
Thereafter	<u>40,276,263</u>
	<u>\$ 45,511,849</u>

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

Notes to Financial Statements

September 30, 2006 and 2005

During fiscal year 2006, the Fund borrowed \$7,026,103 to finance current year direct loan commitments and \$548,371 to meet annual interest payments due to the Treasury Department, at interest rates ranging from 3.55% to 5.47%, depending on maturity dates or risk categories. The Fund repaid \$2,624,516 in principal to the U.S. Treasury from collections of loans receivable.

During fiscal year 2005, the Fund borrowed \$5,828,910 to finance current year direct loan commitments and \$518,541 to meet annual interest payments due to the Treasury Department, at interest rates ranging from 3.55% to 5.47%, depending on maturity dates or risk categories. The Fund repaid \$3,008,090 in principal to the U.S. Treasury from collections of loans receivable and deobligation of a previous loan obligation.

Interest paid for the years ended September 30, 2006 and 2005 was \$2,799,199 and \$2,362,511 respectively.

(5) Commitments

(a) Operating Leases

The Fund leases office space from the General Services Administration in the Homer Building located in Washington, D.C. under the terms of an operating lease which expires in January 2007. This operating lease is in the process of being renegotiated. The Fund also leases equipment under the terms of an operating lease. The total operating lease expense was \$1,350,395 and \$1,115,410 for the years ended September 30, 2006 and 2005, respectively.

Future minimum payments due under these operating leases as of September 30, 2006 were as follows:

<u>Fiscal year</u>		<u>Minimum lease payments</u>
2007	\$	422,823
2008		32,072
2009		29,112
	\$	<u>484,007</u>

(b) Award and Purchase Commitments

As of September 30, 2006 and 2005, award commitments amounted to \$39,112,608 and \$47,836,695, respectively. Award commitments relate to awards which were approved by Fund management but not disbursed as of the end of the year. Award commitments relating to the CDFI Program are not considered liabilities at year-end because the awardees have not met the conditions required for payment. Purchase commitments of \$10,757,159 and \$10,688,518 as of September 30, 2006 and 2005, respectively, relate to the unexpired portion of contracts, and purchase orders relating to goods and services not yet received.

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

Notes to Financial Statements

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(6) Net Position

Net position as of September 30, 2006 and 2005 consisted of the following:

	<u>2006</u>	<u>2005</u>
Unexpended appropriations:		
Unobligated available	\$ 13,820,167	\$ 16,818,726
Unobligated expired	2,585,089	3,650,717
Undelivered orders	<u>47,896,471</u>	<u>46,286,410</u>
Total unexpended appropriations	64,301,727	66,755,853
Cumulative results of operations	30,237,948	40,776,882
	<u><u>\$ 94,539,675</u></u>	<u><u>\$ 107,532,735</u></u>

(7) Other Changes in Net Position

Other changes in net position for the years ended September 30, 2006 and 2005 were as follows:

	<u>2006</u>	<u>2005</u>
Increases:		
Appropriations received	\$ 55,000,000	55,522,000
Appropriation for Subsidy Reestimate	—	479,796
Decreases:		
Appropriation Cancelled	(3,363,017)	(1,891,505)
Appropriation Rescinded	(550,000)	(444,176)
Appropriation Used	(57,431,347)	(69,868,092)
Downward Reestimate Adjustment	<u>(1,488,092)</u>	<u>(497,891)</u>
Total other changes in net position, net	<u><u>\$ (7,832,456)</u></u>	<u><u>(16,699,868)</u></u>

(8) Imputed Financing

Imputed financing represents specific expenses relating to the Fund paid for by another Federal organization. The components of imputed financing for the years ended September 30, 2006 and 2005 are as follows:

	<u>2006</u>	<u>2005</u>
Pension Cost (CSRS Retirement Plan)	\$ 48,894	49,684
Pension Cost (FERS Retirement Plan)	14	2,130
Health Insurance (Health Benefits Program)	226,154	213,280
Life Insurance (Group Life Insurance Program)	722	637
Audit Fees	<u>202,463</u>	<u>80,028</u>
Total	<u><u>\$ 478,247</u></u>	<u><u>345,759</u></u>

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS FUND

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(9) Administrative Expenses

Administrative expenses were significantly higher in fiscal year 2006 than in fiscal year 2005 due primarily to the current year writeoff of \$2.5 million in costs pertaining to internal-use software in development which were carried on the prior year balance sheet as an asset. During fiscal year 2006, the Fund determined that such costs have no future benefit. In addition, administrative costs for fiscal year 2006 includes \$724,782 of software costs considered maintenance as they were incurred subsequent to the placing in service of the related software modules. In the prior year, all software costs incurred were deemed to have a future benefit and so were capitalized.

(10) Shortage of Revenue and Financing Sources Under Expenses

The shortage of revenue and financing sources under expenses for fiscal year 2006 and 2005 includes \$4,252,113 and \$482,075, respectively, of grants and subsidies that were funded from the Fund's no-year account. The no-year account consists of the proceeds from the redemption of investments (see note 3 for a description of the types of investments) as well as income received from these investments.

Pursuant to the Fund's authorizing legislation, the no-year account can be used to fund new awards. Unlike Fund awards that are made out of appropriated funds (which serve to increase grant expenses as well as appropriated capital used and so have no effect on the shortage of revenue and financing sources under expenses), awards funded from the no-year account only affect grant expenses, and so serve to increase the shortage of revenue and financing sources under expenses. Because such amounts funded from the no-year account were significantly higher in fiscal year 2006 than in fiscal year 2005, the shortage of revenue and financing sources under expenses for fiscal year 2006 is significantly higher than in fiscal year 2005.

Appendices

APPENDIX A

APPENDIX A: FY 2006 CDFI FUND AWARD AND ALLOCATION ACTIVITIES

STATE	FA Awards		TA Awards		NI Awards		BEA Awards		Total Awards		Allocation of New Markets Tax Credits (1)	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
Alabama												
Alaska					1	\$100,000			1	\$100,000		
Arizona					3	\$356,750			3	\$356,750		
Arkansas	1	\$585,000					1	\$500,000	2	\$1,085,000		
California	6	\$2,797,122	4	\$346,980	1	\$60,800	3	\$776,225	14	\$3,981,127	7	\$327,000,000
Colorado	2	\$1,085,000			1	\$150,000			3	\$1,235,000	2	\$102,000,000
Connecticut			1	\$42,050					1	\$42,050		
Delaware	1	\$278,731							1	\$278,731		
District of Columbia	2	\$1,085,000							2	\$1,085,000	5	\$455,000,000
Florida	1	\$300,000					1	\$500,000	2	\$800,000		
Georgia							3	\$409,363	3	\$409,363		
Hawaii					2	\$458,000			2	\$458,000		
Idaho	1	\$246,500							1	\$246,500		
Illinois	3	\$1,320,000					6	\$2,560,000	9	\$3,880,000	2	\$160,000,000
Indiana									0	\$0		
Iowa									0	\$0	2	\$105,000,000
Kansas							1	\$12,600	1	\$12,600		
Kentucky	4	\$2,266,000 (3)	1	\$99,895			10	\$628,992	15	\$2,994,887		
Louisiana	3	\$1,467,107	2	\$200,000					5	\$1,667,107	8	\$527,000,000
Maine	1	\$585,000			1	\$320,000 (2)	1	\$145,524	3	\$1,050,524	1	\$120,000,000
Maryland									0	\$0	2	\$155,000,000
Massachusetts	1	\$449,000	1	\$45,000 (5)			3	\$920,000	5	\$1,414,000	4	\$210,000,000
Michigan					2	\$194,500			2	\$194,500		
Minnesota	2	\$685,000	1	\$99,975	2	\$217,300	2	\$1,000,000	7	\$2,002,275	1	\$80,000,000
Mississippi	1	\$585,000	1	\$100,000					2	\$685,000	1	\$15,000,000
Missouri							1	\$500,000	1	\$500,000	2	\$195,000,000
Montana			1	\$80,000					1	\$80,000	1	\$30,000,000
Nebraska									0	\$0		
Nevada									0	\$0		
New Hampshire	1	\$585,000							1	\$585,000		
New Jersey							1	\$340,260	1	\$340,260	2	\$53,000,000
New Mexico	1	\$585,000							1	\$585,000		
New York	6	\$2,305,000	3	\$299,969			4	\$2,000,000	13	\$4,604,969	8	\$623,000,000
North Carolina	2	\$1,170,000	2	\$192,100			1	\$270,000	5	\$1,632,100	1	\$143,000,000
North Dakota									0	\$0		
Ohio									0	\$0	2	\$150,000,000
Oklahoma					1	\$635,000			1	\$635,000		
Oregon							1	\$500,000	1	\$500,000		
Pennsylvania	6	\$2,294,008							6	\$2,294,008	5	\$306,000,000
Puerto Rico									0	\$0		
Rhode Island									0	\$0		
South Carolina			1	\$100,000			2	\$695,741	3	\$795,741	1	\$89,000,000
South Dakota	1	\$585,000			4	\$1,418,333	5	\$159,750	10	\$2,163,083	1	\$50,000,000
Tennessee	1	\$300,000					1	\$75,000	2	\$375,000		
Texas	2	\$1,170,000	4	\$344,440					6	\$1,514,440		
Utah					1	\$128,000			1	\$128,000		
U.S. Virgin Islands									0	\$0		

APPENDIX A: FY 2006 CDFI FUND AWARD AND ALLOCATION ACTIVITIES

STATE	FA Awards		TA Awards		NI Awards		BEA Awards		Total Awards		Allocation of New Markets Tax Credits (1)	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
Vermont	2	\$1,170,000							2	\$1,170,000		
Virginia	1	\$585,000							1	\$585,000	1	\$35,000,000
Washington	2	\$785,000 (4)			2	\$217,000			4	\$1,002,000	2	\$55,000,000
West Virginia									0	\$0		
Wisconsin									0	\$0		
Wyoming					1	\$364,000			1	\$364,000	2	\$115,000,000
Amounts Awarded in FY 2006	54	\$25,268,468	22	\$1,950,409	22	\$4,619,683	47	\$11,993,455	145	\$43,832,015	63	\$4,100,000,000

- (1) Consists of New Markets Tax Credit (NMTC) allocatees headquartered in these states. Amounts shown represent amount of equity to be raised.
 (2) Represents the modification of a FY 2005 award from a grant to a loan; this loan is considered a new FY 2006 award.
 (3) \$600,000 of this amount represents the modification of a FY 2005 award from a loan to a grant; this grant is considered a new FY 2006 award.
 (4) \$200,000 of this amount represents the modification of a FY 2005 award from a grant to a loan; this loan is considered a new FY 2006 award.
 (5) Represents the modification of a prior year award, considered a new FY 2006 award.

APPENDIX B: TOTAL FUND AWARDS FROM INCEPTION

State	FA Awards	TA/SECA Awards	Native Initiative Awards (1)	BEA Awards	Total Awards From Inception	NMTC Allocations (2)
Alabama	\$145,000	\$475,500	\$0	\$615,075	\$1,235,575	\$40,000,000
Alaska	\$7,912,500	\$306,000	\$381,250	\$0	\$8,599,750	\$40,000,000
Arizona	\$5,806,500	\$217,458	\$1,660,250	\$809,288	\$8,493,496	\$235,000,000
Arkansas	\$9,585,000	\$158,514	\$70,000	\$5,075,223	\$14,888,737	\$15,000,000
California	\$50,851,980	\$2,265,707	\$520,706	\$36,234,122	\$89,872,515	\$999,000,000
Colorado	\$8,531,300	\$2,712,358	\$270,000	\$2,116,915	\$13,630,573	\$232,000,000
Connecticut	\$2,883,500	\$542,439	\$0	\$373,205	\$3,799,144	\$0
Delaware	\$923,731	\$122,000	\$0	\$2,751,000	\$3,796,731	\$50,000,000
District of Columbia	\$11,695,983	\$758,800	\$0	\$5,899,454	\$18,354,237	\$1,103,000,000
Florida	\$16,237,000	\$1,256,618	\$0	\$8,991,003	\$26,484,621	\$15,000,000
Georgia	\$3,783,900	\$216,500	\$0	\$6,270,584	\$10,270,984	\$154,000,000
Hawaii	\$1,000,000	\$533,684	\$721,121	\$1,069,199	\$3,324,004	\$28,000,000
Idaho	\$2,793,300	\$200,000	\$0	\$0	\$2,993,300	\$0
Illinois	\$32,797,816	\$1,327,083	\$0	\$32,394,896	\$66,519,795	\$446,050,000
Indiana	\$2,308,000	\$362,500	\$0	\$1,500,651	\$4,171,151	\$81,000,000
Iowa	\$3,990,000	\$265,050	\$0	\$508,500	\$4,763,550	\$149,700,000
Kansas	\$1,903,000	\$240,504	\$25,000	\$2,752,432	\$4,920,936	\$0
Kentucky	\$16,264,163	\$712,995	\$0	\$4,952,028	\$21,929,186	\$153,500,000
Louisiana	\$2,677,107	\$586,050	\$0	\$1,934,109	\$5,197,266	\$949,500,000
Maine	\$12,058,856	\$562,361	\$1,700,000	\$1,481,251	\$15,802,468	\$249,000,000
Maryland	\$14,688,360	\$617,246	\$176,040	\$2,330,221	\$17,811,867	\$801,000,000
Massachusetts	\$18,823,200	\$2,614,345	\$0	\$5,704,405	\$27,141,950	\$562,000,000
Michigan	\$6,115,000	\$260,493	\$548,500	\$1,226,686	\$8,150,679	\$87,000,000
Minnesota	\$16,730,300	\$926,744	\$2,934,833	\$2,754,601	\$23,346,478	\$528,000,000
Mississippi	\$11,811,250	\$226,500	\$0	\$2,029,857	\$14,067,607	\$30,000,000
Missouri	\$1,310,109	\$148,500	\$0	\$4,163,865	\$5,622,474	\$247,000,000
Montana	\$1,446,800	\$524,030	\$716,600	\$315,962	\$3,003,392	\$30,000,000
Nebraska	\$350,000	\$413,843	\$265,000	\$97,832	\$1,126,675	\$23,000,000
Nevada	\$0	\$266,500	\$0	\$339,200	\$605,700	\$0
New Hampshire	\$8,085,000	\$93,425	\$0	\$1,132,000	\$9,310,425	\$0
New Jersey	\$9,265,000	\$706,469	\$0	\$4,587,390	\$14,558,859	\$243,000,000
New Mexico	\$7,188,500	\$97,000	\$0	\$185,705	\$7,471,205	\$0
New York	\$72,281,792	\$6,602,255	\$184,000	\$49,355,326	\$128,423,373	\$1,756,000,000
North Carolina	\$25,706,900	\$1,500,845	\$429,450	\$28,580,498	\$56,217,693	\$553,000,000
North Dakota	\$635,000	\$69,520	\$281,700	\$15,000	\$1,001,220	\$0
Ohio	\$7,881,693	\$992,875	\$0	\$3,743,203	\$12,617,771	\$648,000,000
Oklahoma	\$1,668,500	\$0	\$1,855,880	\$2,365,680	\$5,890,060	\$220,000,000
Oregon	\$5,051,250	\$429,250	\$0	\$5,178,348	\$10,658,848	\$246,500,000

APPENDIX B: TOTAL FUND AWARDS FROM INCEPTION

State	FA Awards	TA/SECA Awards	Native Initiative Awards (1)	BEA Awards	Total Awards From Inception	NMTC Allocations (2)
Pennsylvania	\$33,681,080	\$3,397,986	\$0	\$1,813,327	\$38,892,393	\$353,500,000
Puerto Rico	\$300,000	\$115,000	\$0	\$0	\$415,000	\$0
Rhode Island	\$750,000	\$389,900	\$0	\$0	\$1,139,900	\$0
South Carolina	\$500,000	\$292,600	\$0	\$1,482,524	\$2,275,124	\$89,000,000
South Dakota	\$5,684,810	\$582,000	\$3,483,733	\$722,250	\$10,472,793	\$50,000,000
Tennessee	\$7,265,000	\$150,100	\$95,000	\$3,742,711	\$11,252,811	\$35,250,000
Texas	\$15,654,470	\$3,654,601	\$0	\$15,112,992	\$34,422,063	\$37,000,000
Utah	\$2,000,000	\$392,500	\$353,000	\$120,000	\$2,865,500	\$100,000,000
U.S. Virgin Islands	\$770,000	\$0	\$0	\$0	\$770,000	\$0
Vermont	\$8,999,550	\$490,055	\$0	\$0	\$9,489,605	\$2,000,000
Virginia	\$4,220,400	\$1,023,090	\$0	\$23,000	\$5,266,490	\$106,000,000
Washington	\$7,586,250	\$895,495	\$1,726,800	\$2,405,991	\$12,614,536	\$103,000,000
West Virginia	\$2,439,000	\$331,768	\$0	\$0	\$2,770,768	\$4,000,000
Wisconsin	\$8,729,450	\$293,500	\$797,130	\$2,774,914	\$12,594,994	\$306,000,000
Wyoming	\$0	\$0	\$616,853	\$0	\$616,853	\$0
TOTALS	\$501,767,300	\$42,320,556	\$19,812,846	\$258,032,423	\$821,933,125	\$12,100,000,000

(1) Native Initiative (NI) awards. Consists of awards made under all Native American Programs.

(2) Consists of New Markets Tax Credit (NMTC) allocates headquartered in these states. Amounts shown represents amount of equity supported by tax credits.

APPENDIX C: GLOSSARY OF TERMS

ALLOCATION (OF TAX CREDITS)

Through the New Markets Tax Credit Program, the CDFI Fund provides a Community Development Entity with the authority to sell tax credits to investors in exchange for an investment in the CDE.

BANK

Any organization engaged in any or all of the various functions of banking, i.e., receiving, collecting, transferring, paying, lending, investing, dealing, exchanging, and servicing (safe deposit, custodianship, agency, trusteeship) money and claims to money both domestically and internationally.

In its more specific sense, the term bank refers to institutions providing deposit facilities for the general public, including insured depository institutions. Banking institutions may be classified into two broad groups: (1) commercial banks and their central banks; and (2) noncommercial bank institutions. Included in the latter group are such institutions as savings and loan associations, mutual savings banks, and credit unions. These institutions are often referred to as thrift institutions, although commercial banks also provide savings and time deposit accounts.

BANK ENTERPRISE AWARD (BEA) PROGRAM

Through the Bank Enterprise Award (BEA) Program, the CDFI Fund provides awards to insured depository institutions that increase their level of activities in the form of loans, investments, services, and technical assistance within distressed communities. BEA Program awardees can also provide financial assistance to CDFIs through grants, stock purchases, loans, deposits, and other forms of financial and technical assistance. In general, an award is made based on the lender's success in certain BEA Program-qualified activities that were projected in the application for BEA funds. The BEA Program regulations are found at 12 CFR Part 1806.

COMMUNITY DEVELOPMENT ENTITY (CDE)

Through the New Markets Tax Credit Program, the CDFI Fund certifies an entity as a CDE if it is a duly organized entity that is treated as a domestic corporation or partnership for federal income tax purposes and that (a) has a primary mission of serving, or providing investment capital for, Low-Income Communities or Low-Income Persons; and (b) maintains accountability to residents of Low-Income Communities through their representation on any governing board of the entity.

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTION (CDFI)

Community Development Financial Institution – a nongovernmental entity that meets the following eligibility criteria and is certified by the CDFI Fund as such:

- (i) has a primary mission of promoting community development;
- (ii) serves an eligible investment area or targeted population;
- (iii) has a predominant business activity of providing Financial Products, loans or certain equity investments;
- (iv) in conjunction with its loans or development investments, provides development activities and services that promote community development (ex. financial management technical assistance, financial or credit counseling); and
- (v) maintains accountability to residents of the investment area or targeted population through representation on its governing board or otherwise.

Additional eligibility criteria apply if the entity is a depository institution holding company or an insured depository institution. The CDFI Fund's requirements for CDFI certification and eligibility are found at 12 CFR 1805.200.

COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS (CDFI) FUND

A government corporation within the Department of the Treasury, created to promote economic revitalization and community development through investment in and assistance to CDFIs, including enhancing their liquidity. It was created by Congress and has the duties and responsibilities specified in the Riegle Community Development and Regulatory Improvement Act of 1994.

COMMUNITY INVESTMENT IMPACT SYSTEM (CIIS)

CIIS is a web-based system managed by the CDFI Fund that collects and stores institution-level and transaction-level data from CDFIs and CDEs.

EQUITY

The raising of capital by a corporation issuing or selling its stock (in contrast with “debt,” which is the raising of capital by issuing bonds or borrowing money).

FUNDING ROUND

Each CDFI Fund application and award is identified with a funding round that corresponds to the fiscal year for which the CDFI Fund issues a Notice of Awards Availability (NOFA).

MAPS TO APPS

Newly developed technology that allows Community Development Financial Institutions (CDFIs) and CDFI certification applicants to electronically associate their designated Target Market(s) with an application under the CDFI Program.

NATIVE AMERICAN CDFI ASSISTANCE (NACA) PROGRAM

Through the Native American CDFI Assistance (NACA) Program, introduced in FY 2004, the CDFI Fund provides Financial Assistance awards to eligible Native American CDFIs to support their financing activities, as well as Technical Assistance awards to existing Native CDFIs and Native organizations seeking to become or create a CDFI. A Native American CDFI is de-fined as a CDFI with greater than 50 percent of its activities directed to Native American Communities. In FY 2005, the NACA Program replaced the NACD and NATA Programs.

NATIVE AMERICAN CDFI DEVELOPMENT (NACD) PROGRAM

Replaced by the NACA Program in FY 2005, the Native American CDFI Development (NACD) Program provided Technical Assistance grants to “sponsoring organizations,” such as Tribes or entities primarily serving Native American Communities, to help create Native American CDFIs.

NATIVE AMERICAN TECHNICAL ASSISTANCE (NATA) COMPONENT

Replaced by the NACA Program in FY 2005, the Native American Technical Assistance (NATA) Component was similar to the NACD Program, the difference being that the NATA Component was limited to CDFIs and entities proposing to become CDFIs. NATA grants were provided as part of the Technical Assistance Component of the CDFI Program.

NEW MARKETS TAX CREDIT (NMTC) PROGRAM

Through the New Markets Tax Credit (NMTC) Program, the CDFI Fund provides allocations of tax credits to qualified Community Development Entities (CDEs). The CDEs in turn provide tax credits to private sector investors in exchange for their investment dollars; investment proceeds received by the CDEs are be used to make loans and equity investments in low-income communities.

QUALIFIED EQUITY INVESTMENT (QEI)

An investment in a CDE through the NMTC Program meeting the following criteria: the investment proceeds are used by the CDE to make Qualified Low-Income Community Investments (QLICIs), the CDE designates the investment as a QEI, and the investment is made by the CDE within 5 years from the date of its NMTC allocation.

QUALIFIED LOW-INCOME COMMUNITY INVESTMENT (QLICI)

1) An investment made by a CDE in, or loan to, any qualified active low-income community business; 2) the purchase from a CDE of any such loan; 3) financial counseling and other services to businesses in, and residents of, low-income communities; and 4) any equity investment in, or loan to, any CDE.

TECHNICAL ASSISTANCE

Activities that enhance the capacity of an organization to carry out its business and purpose, such as training of management and other personnel; developing programs and loan or investment loan products; improving financial management and internal operations; and enhancing an organization's community impact.

UNDERSERVED COMMUNITY

An Underserved Community may include the following:

- 1) An Investment Area under the CDFI Program;
- 2) A Targeted Population under the CDFI Program;
- 3) A Low-Income Community under the NMTC Program; and/or
- 4) A Distressed Community under the BEA Program.

Many Native American Communities also qualify as Underserved Communities. "Native American Communities" are defined as any Native American, Alaska Native or Native Hawaiian populations, lands or Census-equivalent entities, with the exception of State or Tribal Designated Statistical Areas.